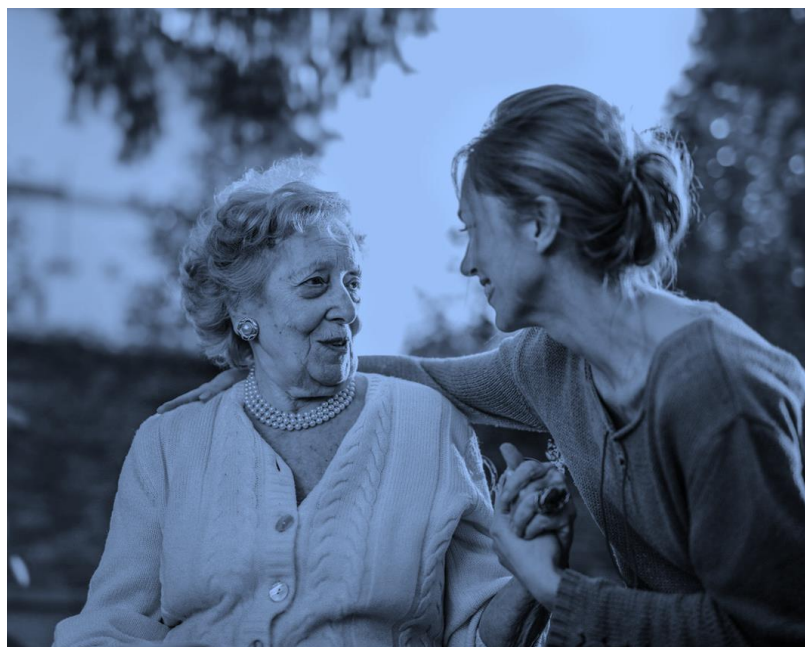


FOCUS

Investment Banking

Healthcare Team

Understanding Investor Interest in Home Healthcare and Hospice



Investment Banking and Advisory Services

FOCUS Investment Banking LLC is a leading Investment Bank with specialized healthcare services expertise. We provide highly tailored services to middle market organizations including:

- Mergers & Acquisitions Advisory
- Corporate Development Consulting
- Strategic Partnering & Alliances
- Capital Financing, Debt & Equity
- Corporate Valuations

September 2021

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Overview of Private Equity's Interest in Home Healthcare and Hospice Agencies

FOCUS Healthcare white papers are designed to provide a clearer picture of M&A activity in key market verticals.

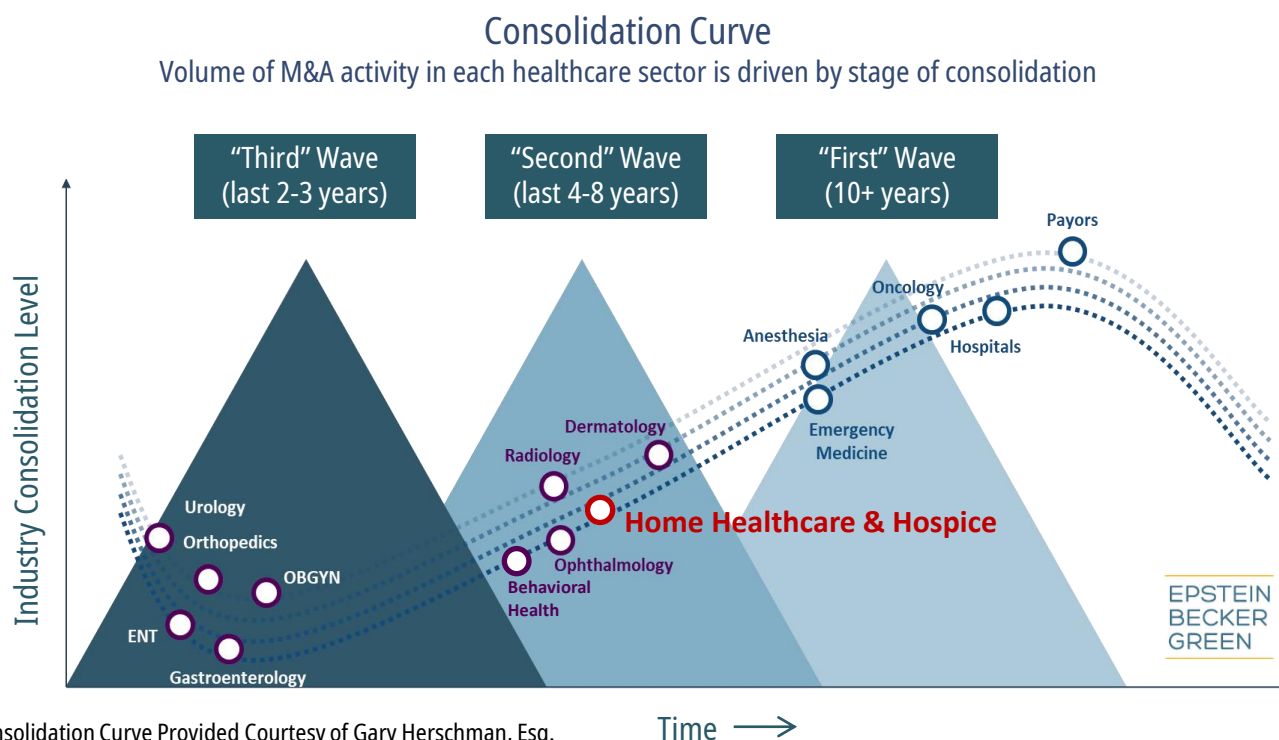
This white paper examines private equity's growing interest in Home Healthcare and Hospice businesses. So far in 2021 there have been 93 reported home health and hospice transactions, a level that exceeds the same period in any prior year. This continues the steady upward trend of M&A activity within the industry. We expect high deal flow throughout the remainder of 2021 and into 2022, supported by increasing private equity interest, a favorable government, and a seller pool that is ready to transact.

Our Clinical Owner Focus

FOCUS Investment Bankers offers an investment banking process designed to deliver great outcomes to clinical business owners embarking on the most important and complex transactions of their lives.

We Specialize in Second and Third Wave Clinical Businesses

We focus on the emerging second and third wave sectors across the full spectrum of clinical businesses. Home Healthcare & Hospice are squarely in the second wave of the consolidation curve characterized by a large volume of smaller add-on acquisitions. Large "platform" agency acquisitions typically occur early and "add-ons" follow. In the second wave, smaller agencies and platform agencies that have yet to be acquired are highly sought after.



Our Closed Transactions

We provide exceptional investment banking services to clinical businesses across the healthcare spectrum.

 **ncgCARE**

HAS ACQUIRED

 **Carolina Outreach**

 **EYE CENTER OF TEXAS**

ACQUIRED BY

 **EYESOUTH PARTNERS**

 **Omni Visions**
Intellectual & Developmental Disabilities

ACQUIRED BY

 **CouncilCapital**

 **Vista SURGICAL CENTER**

ACQUIRED BY

 **SURGERY PARTNERS**

 **MIDWEST VISION PARTNERS**

HAS ACQUIRED

 **Rosenbaum Eye & Laser Center**

 **Arrow CHILD & FAMILY MINISTRIES**
Home & Community Services

ACQUIRED BY

 **MOSAIC**
Real life. Real possibilities.

 **CWC COMPLETE WOMEN CARE**

ACQUIRED BY

 **Women's Care ENTERPRISES**

 **ncgCARE**

HAS ACQUIRED

 **THERAPEUTIC INTERVENTIONS**

 **ncgCARE**

HAS ACQUIRED

 **TPEC**
Turning Point Family CARE

 **Valley Eye Institute**

ACQUIRED BY

 **CIP**

 **ADVOCACY COMPASSION INTEGRITY**
ACI Support Specialists

ACQUIRED BY

 **Dungarvin**

 **Carroll County Surgery Center**

ACQUIRED BY

 **Vision Innovation**
PARTNERS

 **McCoy VISION**

ACQUIRED BY

 **SEES GROUP**

 **ncgCARE**

HAS ACQUIRED

 **GRACE HARBOUR BEHAVIORAL HEALTH**

 **OLYMPIA EYE CLINIC**

ACQUIRED BY

 **NVISION EYE CENTERS**

 **ncgCARE**

HAS ACQUIRED

 **Appalachian COMMUNITY SERVICES**

 **EYESOUTH PARTNERS**

HAS ACQUIRED

 **EYE CENTER OF ST. AUGUSTINE**

Executive Summary

The U.S. home healthcare and hospice industry is expected to grow strongly over the foreseeable future, driven by a variety of demographic and economic trends including a rising elderly population, longer life spans, and more chronic and age-related illnesses. At the same time, a desire for people to live their remaining days in the comfort of their homes benefits the home healthcare industry, which is a lower cost and more personal alternative to the institutional care of hospitals and nursing homes. It is also perceived to be a safer place than these facilities after the Covid-19 pandemic.



There have been close to 100 M&A deals so far in calendar 2021, surpassing the prior year's activity. The home healthcare and hospice business remains a highly fragmented but profitable industry populated by many small, privately-owned players, many of whom are "burnt out" from the pandemic and looking to exit. A recent change in federal reimbursement policies that raises compliance costs by requiring additional staffing, new technology and more capital could also drive out small agency owners unwilling or unable to make those investments. This has

attracted larger players and cash-rich private equity investors, who have driven up business valuations to record levels, which has in turn raised the interest of more providers to sell.

Overview of the Home Healthcare Market

Home Healthcare



The home healthcare market is a large, profitable, and fast-growing industry. The global market is expected to grow at a cumulative annual rate of 7.9% over the next several years, reaching \$515.6 billion by 2027 from \$281.8 billion in 2019 according to a 2020 study by Grand View Research. The report estimates North America's share of that market at 42%, implying a U.S. market size of \$216.6 billion in 2027 up from \$118.4 billion in 2018.

"Population aging around the world and increased preference for value-based healthcare are anticipated to fuel market growth," the report says. "The aging population demands more patient-centric healthcare services, which in turn increases the demand for healthcare workers and agencies and is anticipated to drive market growth."

In the U.S., the market is being driven by "shifting trends towards in-home healthcare from nursing homes, technological advancement, and the presence of advanced medical infrastructure," Grand View says. "Supportive initiatives by the Centers for Medicare and Medicaid Services (CMS) are anticipated to propel market growth further."

According to CMS, \$102.2 billion was spent on home healthcare in 2018. That is expected to increase by about 7% a year through 2027, up from the 4-5% annual increases of the past few years.

According to Health Care Appraisers' 2020 Outlook report, as of 2017 there were roughly 3.4 million Medicare beneficiaries receiving home healthcare services and 1.5 million Medicare beneficiaries receiving hospice services.

"The number of providers in the home health and hospice sector has been steadily increasing since the year 2000," HCA says. "In particular, the number of home healthcare agencies increased from 7,528 in 2000 to 10,785 in 2018. The number of hospice providers increased from 2,255 to 3,864 over the same time period." Much of that increase has been among for-profit entities.

Overview of the Hospice Market

Hospice



The U.S. hospice care market is forecast to nearly double by 2027 to \$56.45 billion from \$29 billion in 2019, a cumulative annual growth rate of 8.6%, according to a recent study by Verified Market Research.

“The rising elderly population, coupled with the increasing prevalence of chronic as well as age-associated diseases, is anticipated to boost growth, as well as a high prevalence of cancer, dementia, and respiratory, cardiovascular, and kidney diseases

among the geriatric population,” the report says.

A competing study from Grand View anticipates even stronger growth. It believes the hospice market will grow at a cumulative annual rate of 9%, reaching \$63.7 billion by 2026 from \$28 billion in 2018, driven by “rising healthcare expenditure, awareness about the benefits of hospices, and favorable reimbursements.”

“Hospice care revenue is expected to rise, despite the uncertainty surrounding reimbursement rates,” said Hospice News, a website that covers the hospice and home healthcare space. “Many people have started using hospice as hospital stays and nursing homes become more expensive. Industry demand will likely escalate alongside the elderly proportion of the population.”

The number of hospice providers increased by 3.7% compounded annually from 3,498 in 2010 to 4,840 in 2019, VMG Health said in its most recent Healthcare M&A report. That growth is being driven exclusively by for-profit providers, which grew by more than 75%, to 3,437 hospices in 2019 from 1,954 in 2010, a compound annual rate of 6.5%. By comparison, the number of non-profit hospices decreased at a compound annual rate of 0.6% while those with government or other ownership structures fell by 4.4% annually over the same period.

Key Catalysts to Continued Growth



“There are many growth drivers impacting the increase in home healthcare expenditures in the United States,” the HCA report says. “Major factors include the aging population, the shift to value-based care and recognition by providers and payors that home healthcare can help reduce readmissions, and the overall push to control costs within the healthcare system. In particular, home healthcare is increasingly being utilized to keep elderly patients in their homes as opposed to assisted-living communities. Home healthcare providers are also being used as an alternative to primary care physicians, and this trend is expected to accelerate as the shortage of primary care physicians is

anticipated to worsen in the coming years. “There are currently more than 40 million seniors in the U.S., and they will account for 20% of the population by the end of this decade, the Institute for Aging says. The fastest-growing segment is those 85 and older, who are expected to total 19 million people by 2050, or 24% of older adults and 5% of the entire population.

“The growing aging population across the U.S., coupled with reimbursement from Medicare and Medicaid and the general shift towards at-home end-of-life care, has impelled the hospice care services market in the U.S.,” KPMG’s May 2020 Hospice Care Services M&A report says. “The expanding population pool of aged people, coupled with increasing caseload of chronic life-limiting diseases, favorable payor environment, and lower costs of care serve as a catalyst for sustainable growth of the hospice care industry.”

The report says about 1.5 million Americans receive hospice care every year, and that the average length of stay rose to 77.9 days in 2019 from 74.5 the prior year, demonstrating “the growing acceptance of hospice care services.”

“With the dramatic increase in the aging population worldwide, the demand for home healthcare agencies is increasing for better patient outcomes,” Grand View says. “In addition, the increasing prevalence of chronic diseases among the elderly is another major factor contributing to market growth.”

Brightstar Care, a home healthcare franchising company, notes that these trends place “mounting pressure on the healthcare industry, including doctors, hospitals, insurance companies and patients. The home healthcare industry relieves the pressure on hospitals, allowing those facilities to focus more on acute care. Home healthcare agencies free up hospitals to tend to patients in more critical condition. Patient preference plays a part in this, with most senior patients preferring to convalesce at home. Home healthcare provides that option and allows hospitals to shift skilled nursing services to home healthcare agencies.”

In addition, “more people are realizing that home healthcare options are less costly and yield better outcomes. Plus, people are simply more comfortable at home, so their outlook is better.”

The COVID-19 pandemic “has had a unique impact” on the post-acute healthcare sector that has led to a shift towards home healthcare and away from institutional facilities such as skilled nursing facilities, VMG notes in its report. “Care in the home health setting provides a lower risk of transmission of the virus,” it said, noting that “approximately 40% of COVID-related deaths have occurred in nursing homes even though only around 8% of COVID-19 cases are attributable to nursing home residents.”

The Impact of Telemedicine

Another important market driver is the recent growing importance of telemedicine in hospice and home healthcare. “The technology is marking its presence to extend its care to outpatient settings to improve care coordination,” Grand View notes.

In 2019, for example, the Hospice of Santa Cruz County in California used a grant from the Central California Alliance for Health “to launch a connected health platform that allows homebound patients and their families to connect with palliative care providers for virtual visits, medication and symptom management and other care,” according to mHealthIntelligence, a website that tracks emerging trends in mobile health, telemedicine, and remote patient monitoring.



“Telehealth is reshaping the home health landscape as providers increase their use of technology to provide better care for patients at lower costs,” HCA says. “Some of the most common applications in the home health space include patient monitoring, medication management, image sharing technology, mobile apps for telehealth consultations with providers, and population health. The ability to provide these services to patients in their homes without sending a provider to the patient represents a significant opportunity for home health agencies to reach more patients, particularly in rural areas or markets with a shortage of providers.”

“Similarly, with recent Medicare expansions in reimbursement for telehealth services, home health will increase in prominence as part of the continuum of care after discharge. Given the steep Medicare penalties associated with patient readmissions, we have observed many health systems utilize home health as a means to treat patients before they require hospital care. Providers are combining chronic care management with remote patient monitoring to provide cost-effective treatment to patients with ongoing serious health conditions.”

As in other healthcare sectors, telehealth utilization in home healthcare and hospice got a boost from the COVID-19 pandemic. “Telehealth and home health are both viewed as effective methods of keeping certain patients out of the hospital, thereby freeing up capacity for dealing with COVID-19,” HCA said.

Understanding the Services Provided



Home healthcare

Home healthcare agencies provide a variety of services, including “patient monitoring, medication management, assessing patient falls, palliative care, identifying diet and nutritional deficiencies, observing mental health, patient education, and functional support such as dressing and feeding patients,” HCA says. Caregivers include nurses, therapists, and social workers, with care coordinated with the patient primary physician.

To qualify for Medicare reimbursement for these services, “the patient must be unable to leave their home without considerable effort, and must require part-time or intermittent skilled care, as certified by a physician.” The patient’s “home” can mean their personal residence, a skilled nursing facility, or an assisted living community.

The home healthcare industry is being boosted not just by the growing number of older people but by the disproportionate amount of care they require. According to the National Council on Aging, nearly 80% of older adults have at least one chronic disease and 77% have at least two. Chronic disease accounts for about 75% of U.S. healthcare spending. The fastest growing diseases among the elderly include Alzheimer’s disease and dementia, cancer, and orthopedic conditions.

Dementia accounted for the largest market share in 2018 and is expected to maintain its dominance, Grand View says. “Dementia is one of the leading causes of mental impairment and dependency among the elderly. Individuals with end-stage dementia become vulnerable to infections, lose awareness, and have increased difficulty communicating, which increases the need for effective care.”

Hospice

Hospice care is generally focused on providing comfort and pain management to patients as opposed to trying to cure an illness. Hospice is generally defined as “healthcare that provides comfort to patients with a prognosis of less than six months to live,” according to HCA. “Hospice care is provided through many of the same types of providers as home health but can also include religious or spiritual counselors and bereavement specialists. Hospice care can also include services outside of traditional medicine, including animal and music therapy.”

Hospice care can be provided in the person’s home, a private hospice facility, a nursing home, or a hospital. Home hospice care is usually less expensive than in outside facilities and provides the patient with the comfort of being home among loved ones.

According to Grand View, hospice centers had the largest market share in 2018, but “home hospice care is anticipated to be the fastest-growing segment owing to growing preference by patients and family members. Home hospice care offers a more comfortable environment and is a more cost-effective option compared to long-term hospital stays.”

Insurance and Reimbursement: A Key Driver of Revenue and Business Success

The Importance of Medicare

Medicare is the largest single payer of home healthcare services in the U.S., accounting for more than 40% of home health expenditures. In addition, “most private health insurance companies include hospice care as a benefit,” Grand View notes. “Some hospices are able to provide services without charge if a patient has limited or no financial resources. Most private insurance plans, health maintenance organizations and other managed care organizations in the U.S. also provide the expenses for hospice care in their plans and policies, which further propel the demand for hospice and palliative care.”

To qualify for hospice care under Medicare, the person agrees that they no longer want care to cure a terminal illness. A hospice doctor or the patient’s doctor must certify that the person is terminally ill, meaning they are expected to have six months or less to live. After six months, the doctor can recertify the patient that they are still terminally ill. Hospice care is usually provided in the home but may also be covered in a hospice facility.



Under Medicare, patients pay nothing for hospice care, which includes all services, including drugs, for pain relief and management; medical, nursing, and social services; medical equipment; aide and homemaker services; and spiritual and grief counseling. There is a \$5 copay per prescription for outpatient drugs for pain and symptom management.

According to the National Hospice and Palliative Care Organization, Medicare spent \$18 billion on hospice services in 2017. In 2018, more than 1.6 million Medicare beneficiaries received hospice care from nearly 5,000 providers. Females account for 58.4% of Medicare hospice beneficiaries, versus 41.6% for males, according to KPMG.

The Recent Shift to the Patient Driven Grouping Model (PDGM)

One of the biggest changes in the industry that is driving market consolidation is the way home healthcare agencies get reimbursed by the government. In a nutshell, the new system requires agencies to continually justify the care they provide before they get paid as opposed to simply providing services, many of which are billed in advance. Or as CMS Administrator Seema Verma said: “The redesign of the home health payment system encourages value over volume and removes incentives to provide unnecessary care. This home health final rule focuses on patient needs and not on the volume of care.

The shift to the Patient Driven Grouping Model is expected to lead to many agencies exiting the industry due to the costs of complying as well as the prospect of lower payments.

The PDGM Tipping Point: Driving Operations Stress and Industry Consolidation

Beginning January 1, 2020, the Centers for Medicare and Medicare Services (CMS) replaced their previous reimbursement model, called the Prospective Payment System (PPS) with a new one, called the Patient Driven Grouping Model (PDGM). The new model “relies more heavily on clinical characteristics and other patient information to place home health periods of care into meaningful payment categories and eliminates the use of therapy service thresholds,” according to CMS. At the same time, the agencies are phasing out Requests for Anticipated Payments (RAPs), in which providers get paid in advance of providing service



“PDGM is expected to dramatically reshape the home health landscape in the coming months and years,” HCA says. “The increasing complexity of the payment model and associated coding and billing requirements are expected to increase costs for providers, particularly smaller agencies, and lead to a period of consolidation within the industry. The large publicly-traded operators have indicated that they expect smaller providers to begin to struggle with the new payment model.”

“Another side effect of the PDGM is the expected layoffs of therapists by home health providers due to changes in the way that therapy services are reimbursed,” HCA said. “Beginning in 2020, therapy services will no longer be reimbursed on a per visit basis but will be reimbursed based on the patient’s clinical characteristics and the complexity of the patient’s needs. As a result, home health operators are expected to (and in some cases already have) lay off therapists as utilization of these services is expected to decline.”

The implications from the shift to PDGM “are likely to affect cash flow and liquidity for smaller home health agencies (HHAs) to a greater extent than well capitalized large operations,” VMA said. “The likely impact is several smaller HHAs will face financial distress and perhaps go out of business. What remains to be seen is whether strategic buyers will capitalize on these opportunities through M&A or by adding resources to existing platforms. For an individual buyer, it will likely be a market-by-market approach. For the industry in general, the likely outcome is an increase in both bankruptcies and M&A volume related to smaller HHAs.”

In addition, “the phase out of RAPs will eliminate the ability of home health agencies to finance operations with payments received prior to the provision of services,” HCA said. “Agencies will therefore have to keep more cash on hand to fund operations.”

Mergers & Acquisitions Drivers

All of the above factors have made the home healthcare and hospice industry an attractive market for investment, both by larger players looking to consolidate and expand as well as strategic investors and private equity firms, which according to some estimates hold more than \$1.5 trillion in unspent capital. This activity has driven up agency values, which in turn has incited many small players to sell, in addition to the other pressures on them to do so. Just through the end of August 2021 there have been close to 100 deals in the space, most of them purchases by larger agencies and PE firms. Smaller agencies have also been induced to sell following a rough 2020, when many were overwhelmed by the Covid-19 pandemic.



“One factor that can’t be ignored is that hospices suffered financially due to COVID,” Hospice News wrote. According to a May 2020 report by the National Association for Home Care & Hospice, about 60% of hospices expected a decline in revenue due to the pandemic, with nearly 30% of them expecting revenue to drop by 15% or more. “Many providers also saw reduced referrals and admissions from hospitals, skilled nursing facilities and senior living operators due to pandemic-related disruption,” Hospice News said.

At the same time, “hospices saw increased demand for personal protective equipment (PPE) and other scarce resources even as prices of those products skyrocketed. A contingent of smaller organizations that tend to see slight margins were unable to take these punches. This moved many of them to sell their businesses to larger companies or private equity firms hungry for a hospice.”



All of which paints a picture of both motivated sellers and eager buyers.

“The industry has garnered significant interest from both private equity firms and strategic investors, and these firms have been very active in expanding their home health and hospice businesses,” KPMG said. “Investors are interested to grow their patient census, add new locations, and enter new geographies. Other investors have entered the space to expand into new service lines and leverage potential synergies. This diverse investor base warrants

greater flexibility and opportunities for home healthcare and hospice companies in a deal process.”

“Investors are also looking to scale their operations, as it is required for the development of an IT platform, drug sourcing, staffing and negotiating. Additionally, growing concerns about the implementation of PDGM in the home healthcare sector has started to shift the focus of investors toward the hospice sector. Further, due to increased competition and a shrinking number of platform opportunities available in the sector, multiples are expected to remain elevated going forward.”

Mergers & Acquisitions Drivers (Continued)

According to HCA, the top 10 home health providers hold a 26.2% market share, while the 10 biggest hospice providers have an 18% market share.

“The need for scale and efficiency, driven by the transition from fee-for-service to value-based payment models and the continued emphasis on outpatient care to reduce healthcare costs, has attracted PE firms to the home health and hospice industry,” the VMG report says. “PE firms targeting home health agencies are looking to take advantage of perceived inefficiencies in site-of-care economic differentials. They aim to capitalize on changing reimbursement models which focus on value of care, rather than frequency of care. Additionally, as Medicare and private insurers continue to push towards lower cost care settings, PE firms aim to capitalize on increasing home health volumes.”

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Another potential driver of deals that affects all industries, not just healthcare, is a proposed increase in the federal capital gains tax rate. That will encourage companies of all types to sell before those changes become effective. If the Biden Administration is successful in raising the tax rate to 43.4% from 23.8% currently, as has been discussed, that could reduce the net proceeds from a sale by more than 20%, according to some estimates. Home healthcare and hospice agencies looking to sell are therefore strongly advised to do so before higher tax rates take effect.

Acquisition Activity Across the US: 2021 To-Date

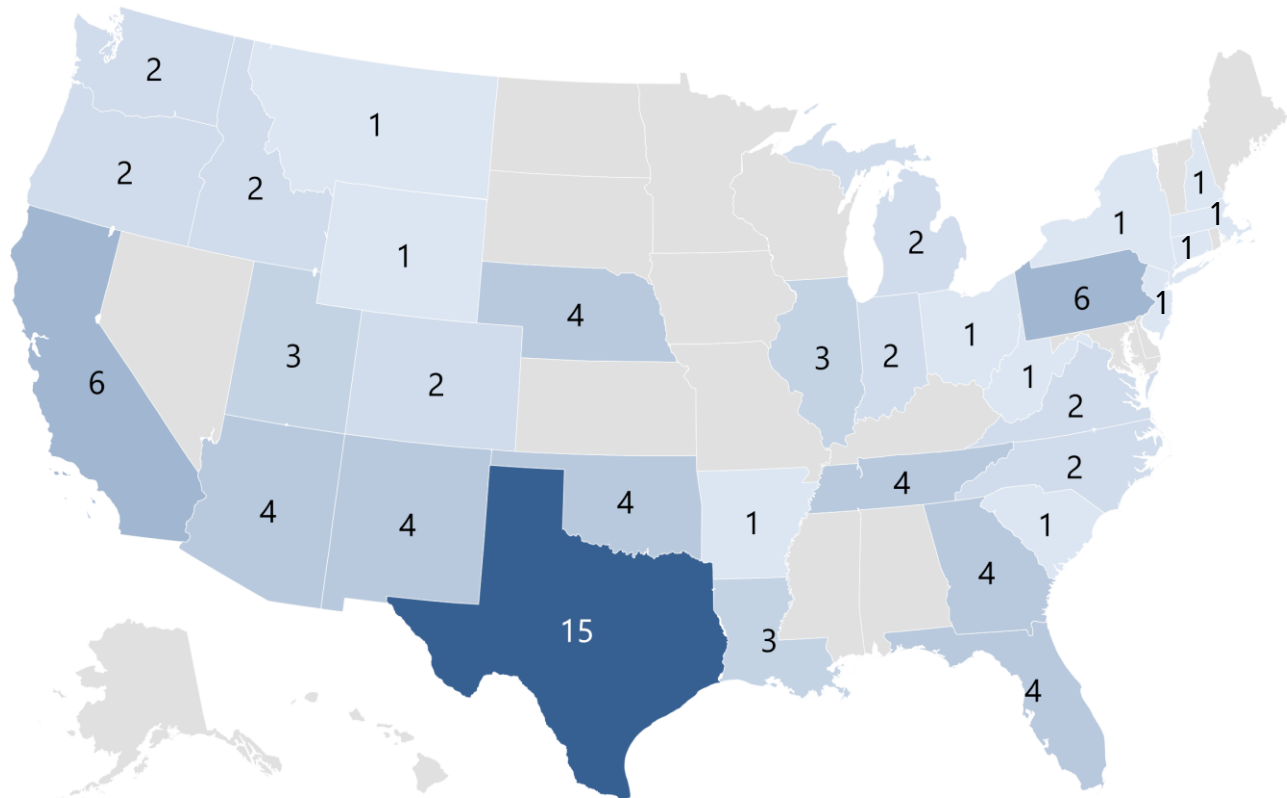
Home Healthcare and Hospice deals were widespread by both geography and buyer for the first eight+ months of 2021. A total of 50 private equity and strategic investors acquired 93 agencies across the US. The most active states were California, Pennsylvania and Texas showing very strong activity.

According to Hospice News, demographic tailwinds have been fueling a thriving hospice market in Texas. The Lone Star State has the third largest elderly population in the nation, according to the Texas Demographic Center, a state institution. The number of Texans 65 or older grew by 49.5% between 2000 and 2014. Only California experienced a higher rate of increase among their senior population.

Florida, Georgia, Tennessee, Oklahoma, Arizona, New Mexico, Nebraska, Louisiana, Utah, and Illinois have shown good deal activity as well.

We expect the acquisition of stand-alone agencies to continue to grow in 2022 We also also anticipate an uptick in investor consolidation to reduce the current count of 50+ buyers. Look for smaller strategic investment companies to merge with larger firms as the industry continues to consolidate.

Home Healthcare and Hospice Deals by State
Jan 1–Sep 8, 2021



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Next Steps for Home Healthcare and Hospice Owners Considering a Sale

If you are considering the sale of your home healthcare or hospice agency, we advise you not to delay, given the reasons cited. FOCUS Investment Banking has a long and successful track record serving middle market firms in the healthcare space.

Working with an investment banker like FOCUS can greatly increase deal value, add choice among buyers, and help protect sellers from unforeseen challenges.

To discuss your specific situation with no obligation please feel free to call:

Eric Yetter
FOCUS Managing Director and Healthcare Team Leader
Direct: 615-477-4741

We are happy to share our knowledge and help you understand your options. All conversations are strictly confidential.

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