

MANAGEMENT

Buyers adjust earnings forecasts



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Q. Are multiples of earnings paid by buyers to acquire a company still in the four to five times range?

A. Most companies today sell, as a multiple, at four to six times the buyers' expected earnings. In calculating their expected earnings, buyers today factor in the effect of the 36-month cap on oxygen and an expected oxygen reimbursement cut based on the results of the first round of competitive bidding. However, to sellers this appears to be a multiple more like two times based on their current results, which do not yet reflect these reimbursement changes. Based on current law, oxygen reimbursements nationwide will drop by 15% to 20% early in 2009 as the first grandfathered patients begin hitting the 36-month cap. Additionally, most industry analysts believe that competitive bidding will reduce oxygen reimbursement rates by a minimum of 20% and that these cuts will be effective nationwide within two years. These reimbursement reductions will have a significant impact on everybody's profits. So a two times multiple of today's earnings can be equal to a five or more times multiple of forecasted earnings. Buyers are simply projecting what they think earnings will look like after the cuts. Another change we are seeing is a tendency for buyers to focus more on cash flow, instead of EBITDA. Increasingly, we see buyers modeling cash flows after a provision for the cost of capital expenditures such as rental equipment as the basis for their multiple. If owners considering a sale think buyers are being overly pessimistic, it makes sense to postpone a transaction until current laws (and buyer models) catch up to their vision of a world with no oxygen caps or additional rate cuts. **HME**

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