



The Future of Healthcare Funding: From Traditional to Disruptive Models

Lone Star HFMA 2025 Winter Conference

January 30, 2025

Funding Cycle Overview

Cycle of Funding Over Business Life

The “J-curve” plots an investment’s hypothetical performance over time where the shape of the plot initially dips negative then recovers



Healthcare Investor Overview

Early-stage investments are defined by revenue growth and equity financing; later stages focus on profitability, cash flows, and the effective use of leverage

	Early Stage / Venture	Growth / Scaled Capital	Public Equity / Debt / Funding Vehicles
Select Market Participants	▪ Angel Investors / Crowdsourcing / Grants ▪ Early-Stage VC	▪ Late-Stage VC ▪ Growth Equity	▪ Private Equity ▪ Public / Private Lenders
Average Investment Size	▪ < \$25M	▪ ~\$5M to ~\$100M	▪ ~\$100M to \$1B+
Target Investment Criteria	▪ Disruptor technology / business model ▪ Significant white space in the market ▪ Management team you are willing to bet on	▪ Clear strategies for expansion and scalability ▪ Emerging competitive positioning in a strong underlying market ▪ Management team has shown strong historical success, have similarly aligned growth aspirations	▪ Stable cashflows that can be used to support debt balances / leverage ▪ Strong, established market positioning, competitive moat, customer relationships, and management
Strategic Goals	▪ Focus is often on rapidly gaining market share, potentially at the expense of profitability ▪ Develop a robust value proposition and brand name ▪ Sell the story to future rounds of investors	▪ Expand the focus on profitability; prove general business viability at scale ▪ Continue to grow the top-line, targeting new markets and cross-selling products ▪ Provide secondary liquidity to shareholders	▪ Execute an operational playbook, which can span from top-line growth initiatives to cost cutting for margin improvements ▪ Position the business for a successful exit through an acquisition or public offering
Key Growth Areas	1) Business Model 2) Addressable Market	1) Revenue 2) Path to Profitability	1) EBITDA / Net Income 2) Revenue
Financing Structure	▪ Equity financing only – Sell potential investors on the upside potential (i.e., strong equity returns) for this company	▪ Majority equity financing – Financing rounds typically increase in size for each series ▪ Debt financing available but limited – Asset-based private lending – Opportunity for cash flow lending with scale	▪ Availability of both equity and debt financing – Optionality to access the public equity and debt markets, exposing the company to a wider investor base – Cash flow lending available ▪ Several other bank products available

Select Healthcare Investors

Several health systems, including Providence, have venture arms and pursue opportunistic M&A at the parent-level

Private / Growth Equity



Venture Capital



Health System w/ Venture Arms



Healthcare Funds – Capital Flows

Difficult M&A conditions and reset valuations have led to fewer exits, less capital returned to LPs, and difficulties fundraising

Fundraising

- GPs pitch to LPs for capital
- Key considerations around track record, investment type, and deployment strategy
- **Will increase dry powder**

Limited Partners (LPs)

Return of Capital

- Cash will be returned to GPs and LPs through asset / equity sales, dividend payments, or mgmt. fees
- In 2023, the top US PE exits were acquisitions by corporates (~56%), acquisitions by sponsors (~41%), and public listings (~3%)
- How capital is returned to LPs and GPs is determined by the designated hurdle rate for the fund

General Partners (GPs) /
Financial Sponsors

Target Companies
(PortCos)

Capital Deployment

- Equity capital is put to work in acquiring minority or majority stakes in target companies
- Typically, will be represented in the form of M&A / LBO volumes for private equity firms
- **Will decrease dry powder**

Key Terminology

- **Limited Partners:** Investors into funds, often external and with significant capital amounts; have no management responsibilities for the fund (e.g., a pension or sovereign wealth fund investing in a private equity fund)
- **General Partners / Financial Sponsors:** Partners that execute the capital deployment and management of a fund (e.g., venture capital, growth equity, and private equity firms)
- **Dry Powder:** Capital that is available to be deployed within a fund; this figure is calculated based on the amount of fundraising achieved (cash inflows) and capital deployed (cash outflows)
- **Portfolio Companies (“PortCos”):** Companies that have received equity investments from a financial sponsor

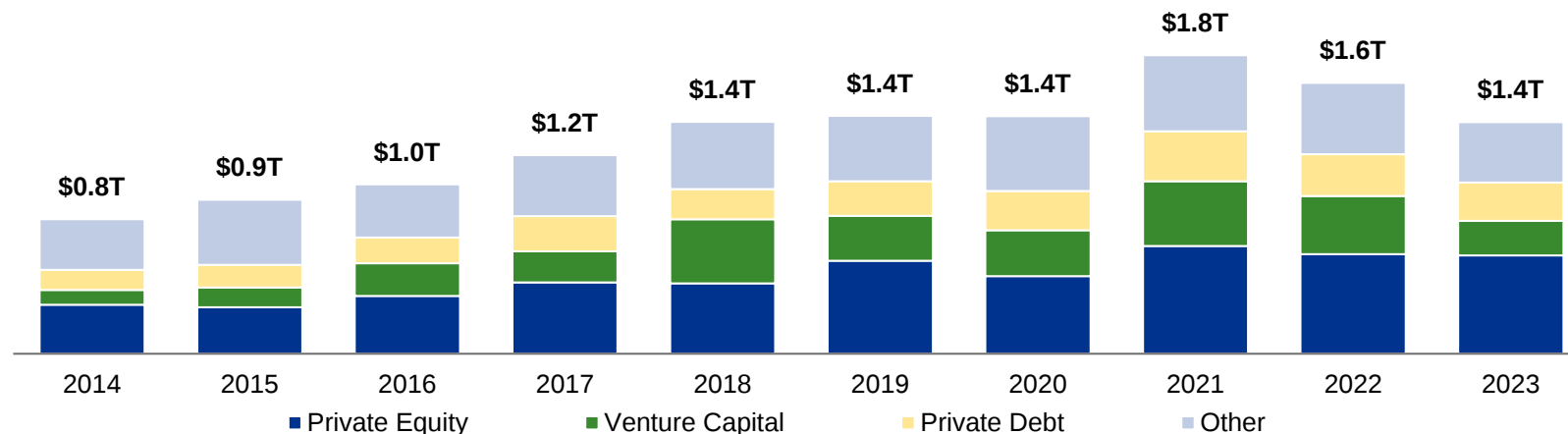
Recent Dynamics

- **Since its 2021 / 2022 peak, the flywheel has significantly slowed across all investment types (i.e., VC, growth equity, PE)**
 - With reduced exits, sponsors have returned less capital to LPs
 - This has led to difficulties for many sponsors seeking to raise capital for new funds... they may be seeking money from LPs who have not yet received distributions from their last investment
- **M&A markets have stagnated** due to buyer-seller valuation gaps, a high-interest rate environment (increased the cost of capital), strategics buyers prioritizing balance sheet strength and credit ratings, and difficult company-level operating dynamics
- **Equity valuations have been reset**, as seen in the share price declines from 2021 IPOs / SPACs; this has flowed to the VC market with many investments worth less than their valuation at the prior funding round

There Remains a Significant Amount of Available Dry Powder

Private equity, venture capital, and private debt dry powder levels remain near record highs due to high fundraising amounts since 2018 and slowed capital deployment

Although Fundraising has Cooled in Recent Years...

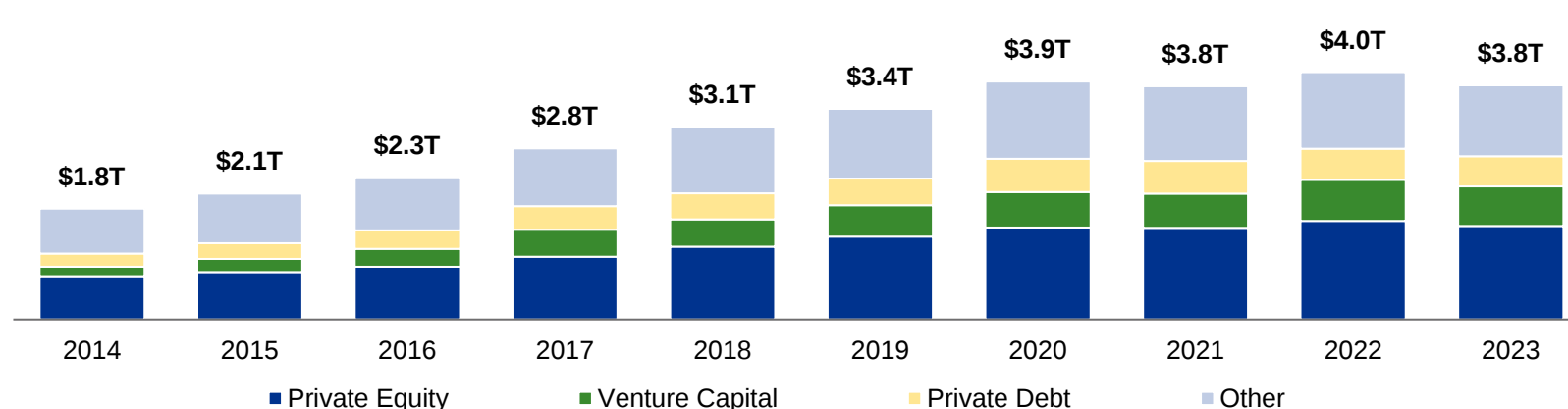


+26%
Change '19 to '21

(22%)
Change '21 to '23

(3%)
Change '19 to '23

...Dry Powder Amounts Remains Robust



+11%
Change '19 to '21

~0%
Change '21 to '23

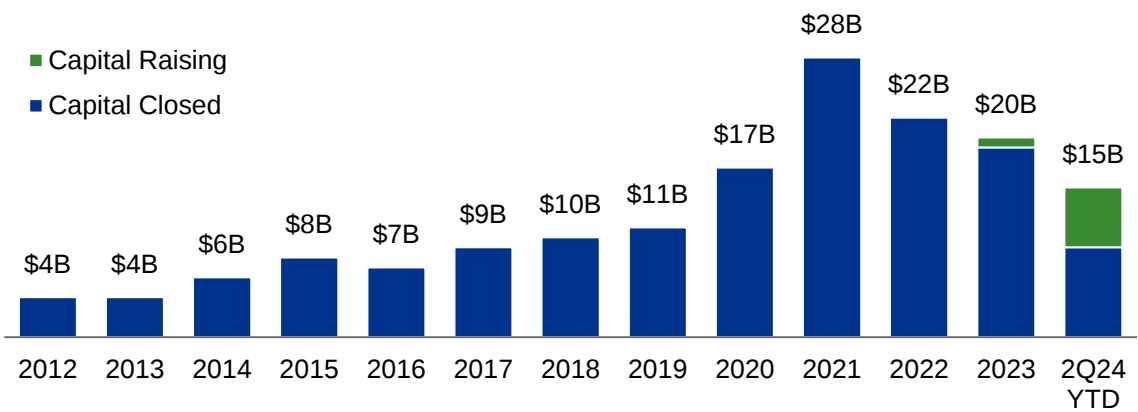
+11%
Change '19 to '23

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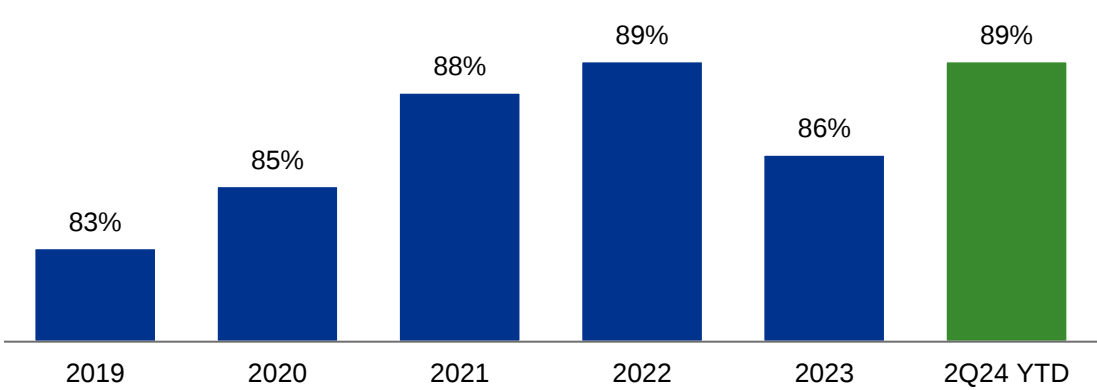
Healthcare Venture Capital is Recovering

While healthcare VC fundraising remains well below 2021 peaks, signs of recovery are emerging (e.g., higher percentages of funds hitting their targets, recent increases in deal counts and dollars deployed, etc.)

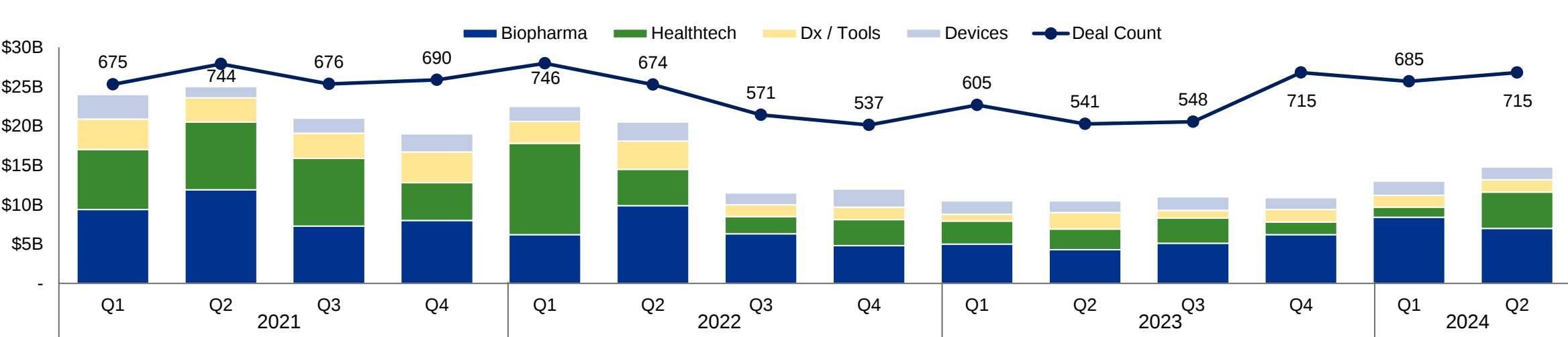
US Healthcare VC Fundraising has Begun to Recover in 1H24



US Healthcare-Focused VC Funds That Hit Their Target



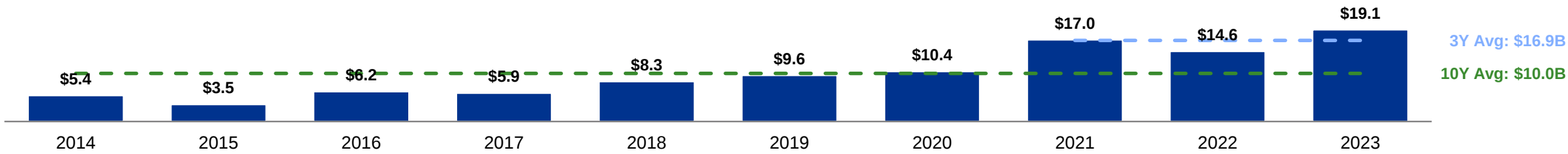
VC Dollars and Deal Count by Healthcare Sector (US, EU, UK)



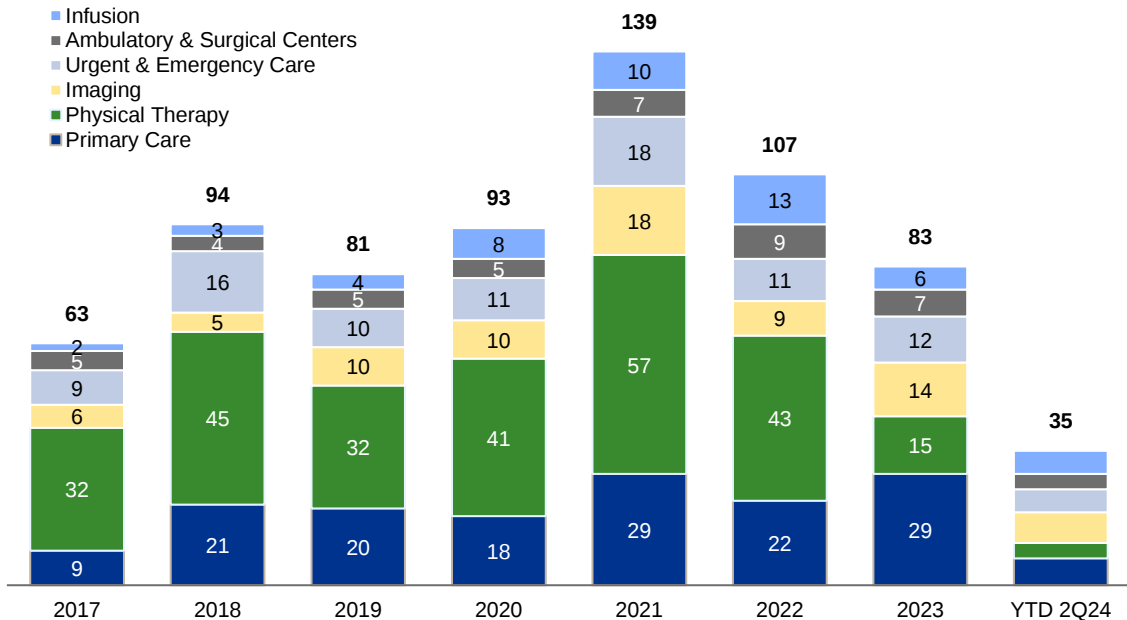
Financial Sponsors Remain Active Participants in Healthcare Services

Healthcare-focused PE firms continue to raise money at record clips; with capital deployment slowing, sponsors are sitting on significant dry powder that should provide a tailwind for asset valuations

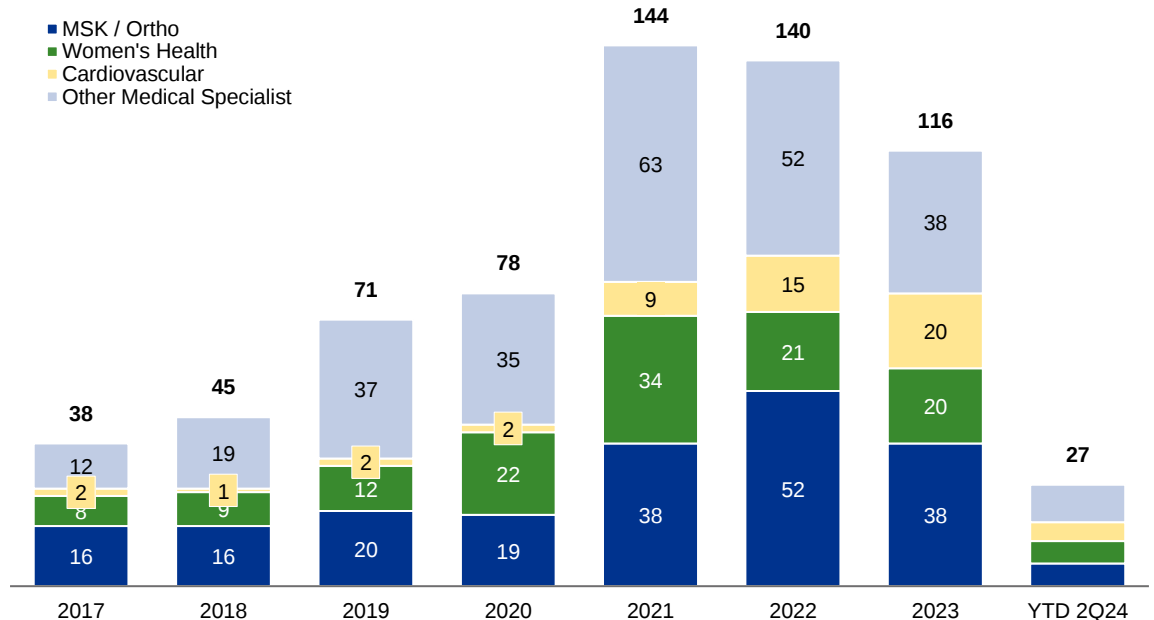
Healthcare-Focused PE Fundraising (\$B)



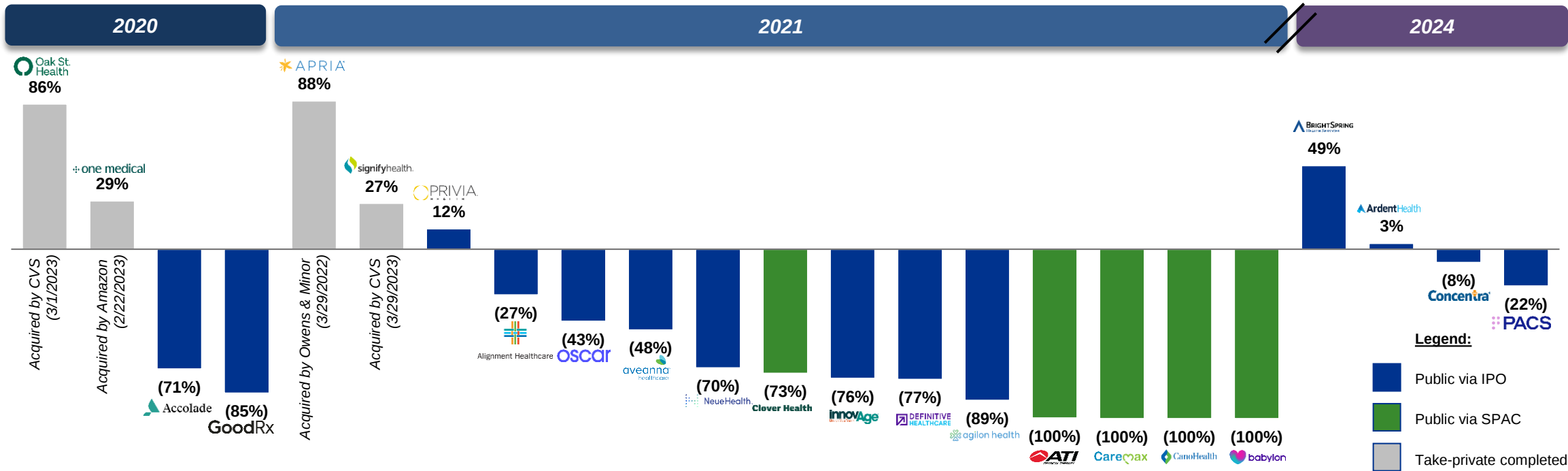
Alternative Site Deal Cadence (# deals)



Specialty PPMs¹ Deal Cadence (# deals)



2020 & 2021 IPOs in Healthcare Services Have Underperformed; 2024 Cohort has Outperformed to Date

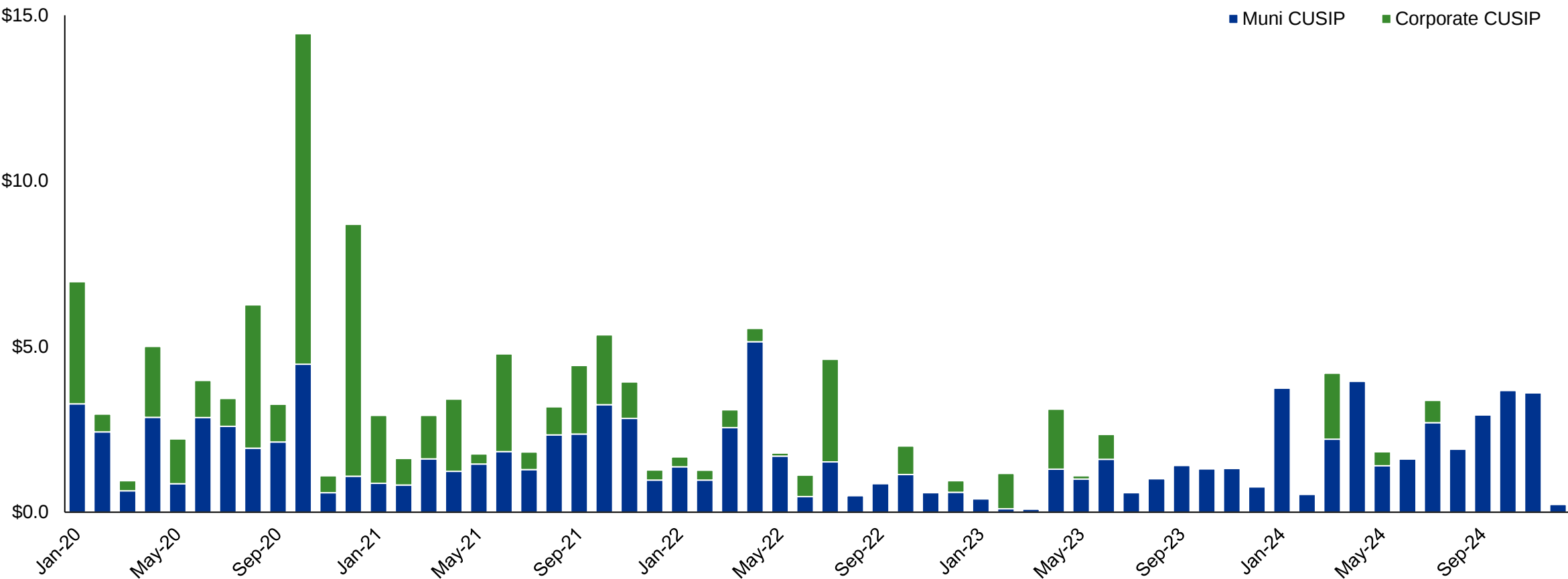


Commentary

- Many of the IPOs and De-SPACs from 2020 – 2021 were companies with long-tail business models, which are reliant on low-cost access to capital
 - Since then, costs of capital have increased and the benefits of being public have diminished, pressuring company performance and share prices
- Several companies that went public from 2020 – 2021 have since been acquired by strategics, including Oak Street Health and One Medical
 - While other sectors have seen significant take-private interest for 2020 – 2021 public listings, including many at below listing price, healthcare has predominantly seen its M&A interest from strategics targeting top-tier assets
- The remaining public companies from the 2020 – 2021 cohort have largely traded down since IPO / SPAC; SPACs have underperformed IPOs
 - Several have lost < 90% market value since they went public, including bankruptcies such as Cano Health (Ch. 11), CareMax (Ch. 11) and Babylon (Ch. 7)
- In 2022 – 2023, there were no notable healthcare services public offerings due to market conditions and the poor performance of the 2020 – 2021 vintage
- The IPO market has re-opened in 2024 with PACS, BrightSpring, Ardent, and Concentra going public

Not-for-Profit Healthcare Debt Markets in 2024

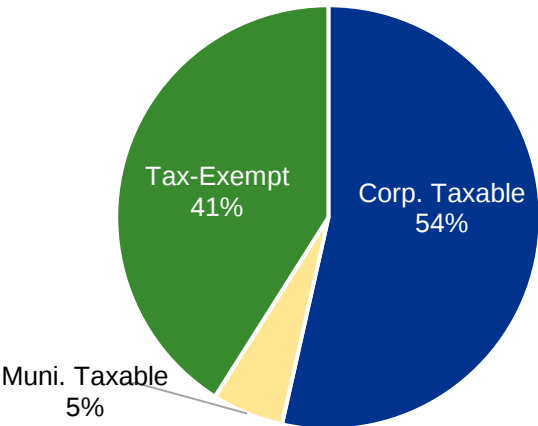
2024 monthly new issue supply by not-for-profit healthcare systems averaged \$2.8 billion following an average of \$1.2 billion during the same period in 2023



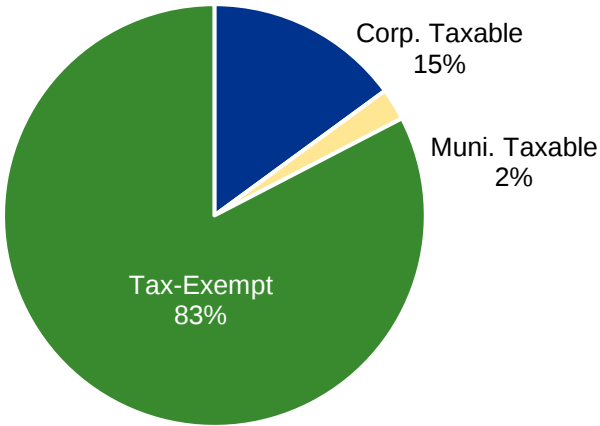
Not-for-Profit Healthcare Debt Markets in 2024

Since the start of 2023, new issuance among health systems has favored the short and intermediate tenors

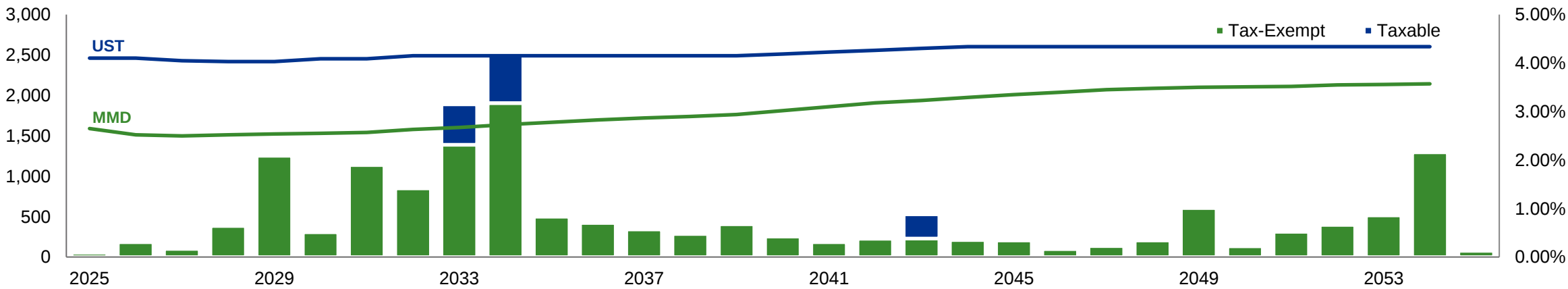
2020 NFP HC Issuance by Tax Status



2024 NFP HC Issuance by Tax Status



Selected Healthcare Primary Market Issuance Since January 2023⁽¹⁾



Healthcare Sector Review

Overview of US Healthcare Spending & Industry Dynamics

Overview of U.S. Healthcare Spend

\$4.9T

2023 National Health Expenditures

+7.5%

YoY Growth in NHE in 2023

~17.6%

NHE as a % of US GDP (2023)

~31%

Hospital Care as a % of NHE

- National health expenditures (“NHE”) totaled \$4.9T in 2023, representing ~17.6% of United States Gross Domestic Product (“GDP”)
 - This figure has grown by 7.5%, 4.6%, and 3.2% in 2023, 2022, and 2021, respectively
 - Hospital Care grew by 10.4% in the year, its fastest rate of growth since 1990, driven by an increased number of discharges and increased Medicare outpatient hospital utilization
- The CMS projects that NHE will reach ~20% of U.S. GDP by 2032
 - National health expenditures are anticipated to grow at a +5.6% CAGR from '23 to '32

Key Trends Shaping U.S. Healthcare



Aging Population



Expansion of Virtual Care



Prescription Drug Pricing



Price Transparency Requirements

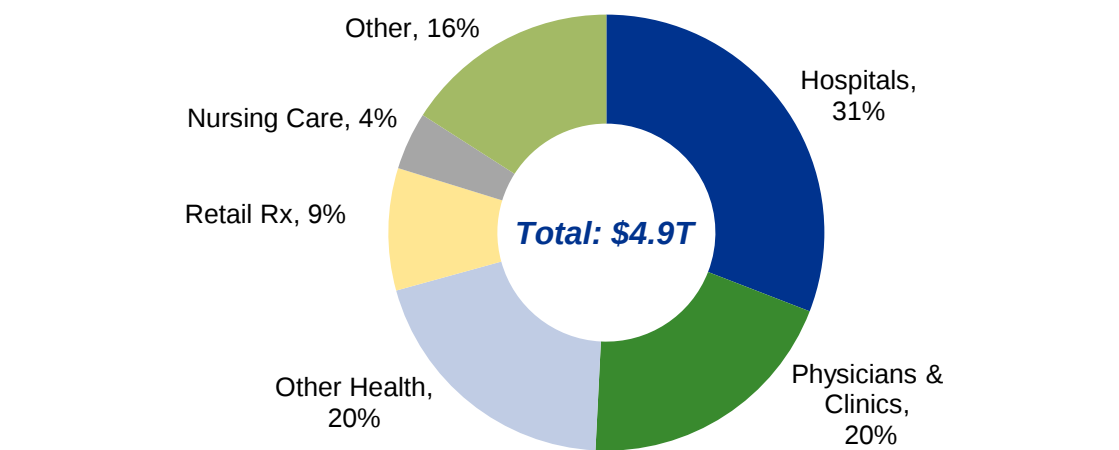


Value-Based Payment Models

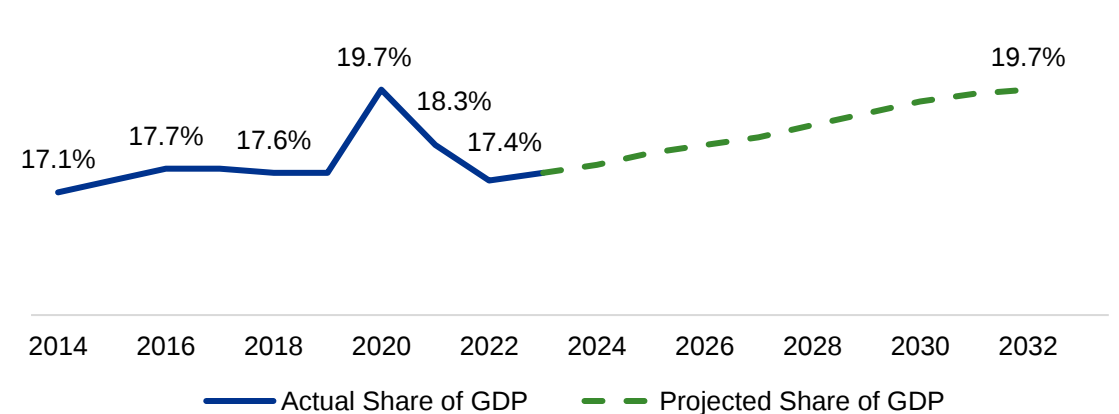


Changes in Government Plan Coverage

Hospital & Physician Services Represent ~50% of Spend (2023)

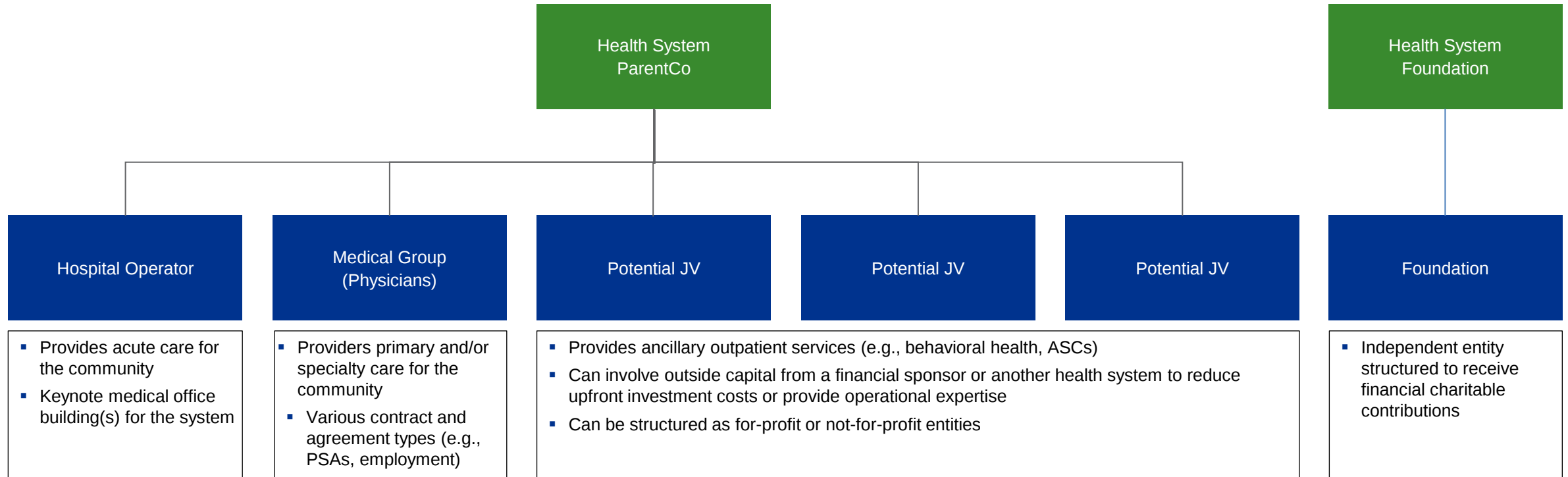


NHE as a Percentage of U.S. GDP (2014 - 2032)



Health System Organization Structure

Illustrative Health System Org Chart



How Do Health Systems Have “Equity”

- Since health systems are not-for-profit entities, they do not have equity in the traditional sense (i.e., public company stock, ParentCo ownership by equity investors)
- Moreover, Health system equity can be thought of as the various assets that a system can monetize, including their real estate, joint ventures, and outreach labs
 - A health system faces the continual balance of where to allocate its resources, and the sale of select assets can free up capital to be deployed in other strategic priorities for the business
 - Additionally, a sale can allow management to redeploy their focus and resources towards other areas

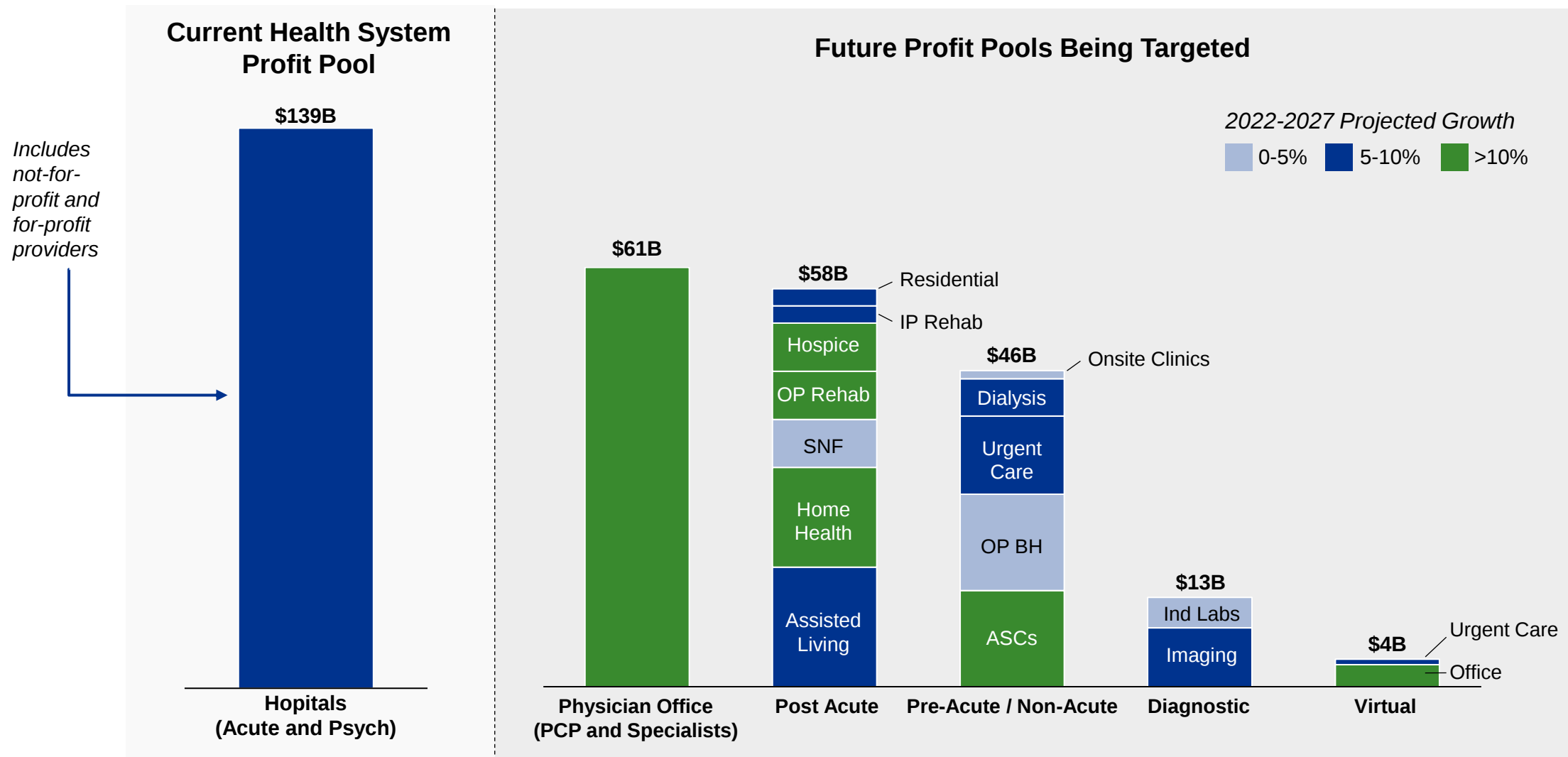
Healthcare Segments



	Pharmaceuticals and Biotech	Health Technology	Medical Devices	Payors / Managed Care	Providers
Description	Produces drugs, vaccines, and other products that help users recover from injuries, and treat illnesses	IT tools/software designed for hospital and administrative productivity, give new insights, or improve care	Products ranging from surgical gloves, prosthetics, imaging equipment, and more – can also include diagnostics test kits or lab reagents	Health insurance companies or gov't entities that pay for health services and care	Range of services includes primary care, behavioral, OB/GYN, surgery centers, spine, emergency & more
Investment Types	VC / Public Equity (IPOs)	VC / Public Equity (IPOs)	Public / Private Equity	Public / Private Equity Buyout / LBO	Public / Private Equity Buyout / LBO
U.S. Market Size	\$600B	\$600B	\$500B	\$1.4T	\$2.2T
Market Consolidation Status	Fragmented	Fragmented	Consolidating	Highly Consolidated	Consolidating
Select Key Players					

Analysis of Provider Sub-Segment

While Acute Care Continues To Be The Largest Single Profit Pool, Providers are Diversifying and Scaling in New Profit Pools with Higher Projected Growth



Diving into Not-For-Profit Hospitals and Health Systems

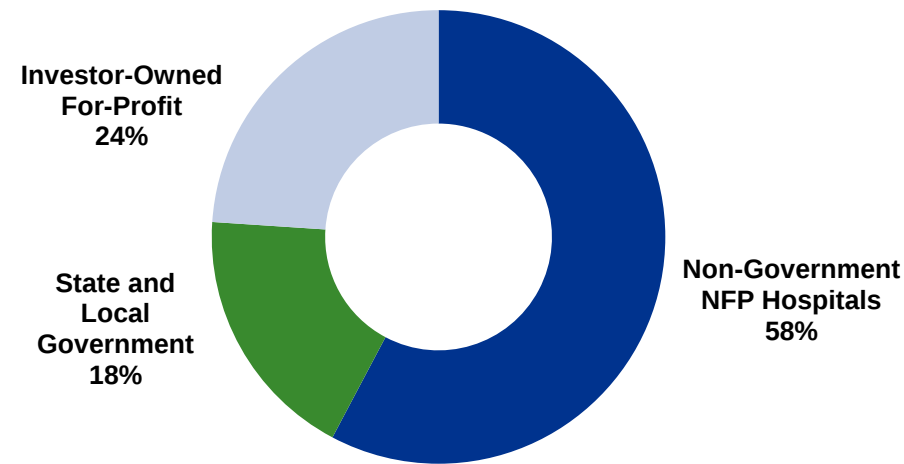
Overview of Not-For-Profit Hospitals and Health Systems

- Not-for-Profit (NFP) hospitals are healthcare organizations that operate with the primary aim of providing medical services to the community, rather than generating profit
- They are exempt from paying federal, state, and property taxes, due to their status as 501(c)(3) non-profit organizations under the IRS tax code
- NFP hospitals typically operate with a board of directors, rather than a group of owners or shareholders, and any surplus revenue generated by the organization is reinvested back into the hospital to improve patient care and services
- NFP hospitals are often involved in charitable and community outreach programs, providing medical care to underserved populations and contributing to the health and well-being of the communities they serve
 - Evident by the relatively large portion of government payers within their revenue mix
- Some NFP hospitals may also have religious affiliations, with a mission to serve their communities in accordance with their beliefs and values

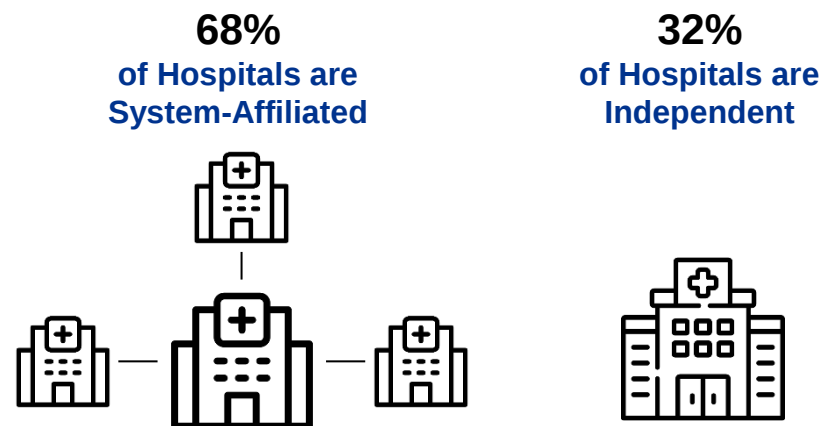
Key Differences Between Not-For-Profit and For-Profit

Category	Not-For-Profit (NFP) Hospitals	For-Profit (FP) Hospitals
Ownership	Governed by a board of directors	Corporations owned by investors
Profit Distribution	Cannot distribute profit to those who control the organization	Can distribute some proportion of profits to owners
Tax status	Generally, exempt from taxes	Pay property, sales, income taxes
Funding Sources	Charitable contributions, tax-exempt debt, retained earnings (including depreciation), government grants	Equity capital, taxable debt, retained earnings (including depreciation and deferred taxes)
Purpose	Has legal obligation to fulfill a stated mission (provide services, teaching, research)	Has legal obligation to enhance the wealth of shareholders within the boundaries of law; does so by providing services

~80% of US Hospitals are Not-For-Profit 501(c)(3) Organizations



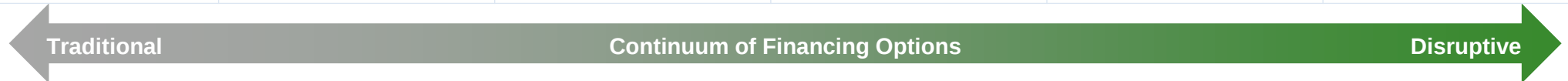
68% of US Hospitals are Health System-Affiliated



Healthcare Financing Options

Funding Sources Range from Traditional to Innovative

	Philanthropy	Tax-Exempt Debt	Taxable Corporate	1 Private Debt Markets (Private Placement, Credit Lending, etc.)	2 Non-Core Asset Monetization	3 Joint Ventures / Partnerships
Description	Charitable donations that serve as an additional revenue stream, occasionally earmarked to advance specific goals such as health equity and access	- Issue public tax-exempt debt through conduit issuer into the primary market - Useful if preference for amortizing structure	- Issuing public taxable debt into the primary market, typically in a bullet maturity structure - Optimal for sizeable borrowing needs	- Issuing private taxable debt to a targeted investor base or a private bank lender - Optimal for product customization	- Dispose of non-core assets, such as real estate or central utility plant, to refocus financial and management resources - Can take form of sale, partnership, or strategic affiliation	Joint venture with private company to sell, acquire, or develop a specific service line or capability
Investor Base	Foundations, Individuals	Muni-eligible funds, SMAs, and retail	Domestic and international, potentially larger buyer base	Domestic and international investors, private banks	Strategics / Sponsors	Sponsors
Tenor	Varies	Long Term	Long Term	Long Term	Long Term	Medium Term
Benefits and Considerations	✓ High ROI, zero-cost funding mechanism that complements revenue streams ✓ Increase debt capacity and improve credit metrics ✗ Potentially limited capital pool, requiring replenishment ✗ Short-to-medium-term financing vehicle ✗ Subject to macroeconomic trends	✓ Lower cost with ability to amortize across the curve ✓ Accommodative market to various sizes ✓ Long-term financing solution ✗ Pressures debt capacity and credit metrics ✗ Requires conduit issuer, adding complexity/time ✗ Must find eligible projects	✓ Ease of execution, no conduit approval needed ✓ Large, deep investor base ✓ Ability to reopen CUSIP for additional financing at later date ✗ Pressures debt capacity and credit metrics ✗ Higher cost option than tax-exempt market ✗ Preference for bullet structure, no amort.	✓ Greater flexibility and control of financing ✓ Ease of execution, no conduit approval needed ✓ More confidentiality versus public debt options ✗ Pressures debt capacity and credit metrics ✗ Higher cost option than tax-exempt market ✗ Lack of liquidity	✓ Narrows management focus to core operations ✓ Increase debt capacity and improve credit metrics at parent level ✗ Potential degradation of care quality ✗ If required, physician buy-in can present a challenge	✓ Maintains use of the assets while receiving cash upfront ✓ Increase debt capacity and improve credit metrics at parent level ✗ Potentially costly financing option to meet fund's return hurdle ✗ Medium-term financing vehicle



1 Case Study | Providence St. Joseph Health 4(a)(2) Private Placement



\$383,000,000

Series 2023
Senior Notes

Maturities:
10/1/2028
10/1/2033
10/1/2043

Closed February 2023

Final Terms	5-Year	10-Year	20-Year
Par Amount:	\$383,000,000		
Maturity:	Oct. 1, 2028	Oct. 1, 2033	Oct. 1, 2043
Structure:	5-Yr Bullet	10-Yr Bullet	20yr / 15yr WAL
Tranche Size:	\$110,000,000	\$85,000,000	\$188,000,000
Coupon:	5.42%	5.45%	5.71%
Pricing Date:	Feb. 8, 2023		
Closing Date:	Feb. 21, 2023		
Opt. Redemption:	Make-Whole Call		

Key Features of 4(a)(2) Private Placement	
Primary Buyer Base	Life Insurance Companies (i.e. New York Life, MetLife)
Issuer Market Access	Investment Grade
Time from Mandate to Funding	~5 weeks
Average Syndicate Size	1-10 Buyers
Size for Best Execution	Ample Capacity to Add Additional Debt per Investor Interest
Structure for Best Execution	Bullet & Amortizing
Term for Best Execution	1-30 Year Term
Funding Committed to Maturity	✓
Forward Settlement Premium	< 90 Day Forward: 0 bps 90-365 Day Forward: 5-10 bps
No Official Statement	✓
No Appendix A	✓
No Investor Presentation	Management Update Call Only
Credit Rating Requirement	Up To 12 Months After Pricing With No Penalty
Investor Dialogue	Immediate
Covenants In Excess of MTI	Replicate Existing Provisions of Existing Note Purchase Agreement

Transaction Summary:

- On February 8, RBC Capital Markets served as placement agent on a \$383,000,000 Section 4(a)(2) taxable private placement for Providence St. Joseph Health ("Providence"). The par amount was split between \$110 million 5-year taxable bullet, \$85 million 10-year taxable bullet, and \$188 million 15-year taxable weighted average life ("WAL") structure
- Proceeds from the issuance used to redeem a portion of Providence's outstanding revolving line of credit
- RBCCM as placement agent included some of the largest institutional buyers in a negotiated process, ultimately allotting the notes to 12 investors across 3 tranches with 5-to-20-year terms

2 Case Study | Adventist Health Energy as a Service (EaaS) Partnership

Energy-as-a-Service Partnership



Upfront Cash Consideration to
Adventist:

\$457,200,000

Closed June 2024

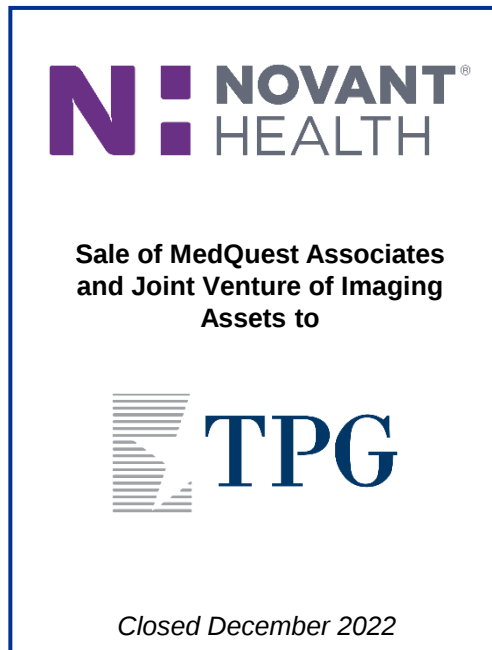
Partnership Overview

- Adventist Health System/West ("Adventist"), a 28-hospital not-for-profit system based out of Roseville, California with operations in California, Oregon and Hawaii closed its 30-year enterprise-wide Energy-as-a-Service partnership with Bernhard in June 2024
- The partnership is the first EaaS transaction to deliver the upfront Advance Lease Payment on a tax-exempt basis (publicly offered) yielding significant economic benefit to Adventist
- Adventist's guiding principals through development of their Energy-as-a-Service partnership were to:
 - Capture significant Operating Expense savings leading to material P&L benefit; then
 - Leverage and reinvest these savings across the system in critical deferred CapEx and resiliency needs all while maintaining an EBIDA neutral outcome
- Despite capitalizing with tax-exempt proceeds, Adventist recognized no incremental debt on its Balance Sheet as a result of the Energy-as-a-Service partnership
- By engaging in Energy-as-a-Service, Adventist has successfully preserved its debt capacity for higher yielding, core mission focused initiatives

Commercial Transaction Highlights

- Partnership Term:** 30 Years
- States:** California, Oregon, Hawaii
- Upfront Cash Consideration to Adventist:** \$457.2mm | Value extracted from right to operate and utilize excess capacity of existing chilled water and steam system capacity at nine hospitals
- Book & Title Ownership of Subject Assets:** Retained by Adventist
- Purchased Electricity:** 61.1% reduction at flagship
- Scope 2 GHG Emissions:** 63.7% reduction at flagship
- Guaranteed Utility Expense Savings:** ~20% in Annual Utility Spend

3 Case Study | Novant Health Sale of MedQuest Associates to TPG



Transaction Highlights:

- In December of 2022, Novant Health announced the formation of an innovative joint venture partnership with TPG to create a national diagnostic imaging platform to serve as the partner of choice for health systems
- Under the newly-created joint venture partnership, Novant Health will contribute MedQuest Associates (“MedQuest”), a leading owner, operator and manager of diagnostic imaging facilities with a network of over 50 imaging centers under management

“Leveraging the comprehensive capabilities of MedQuest and TPG's business-building aptitude, joint venture experience, and health system relationships, this partnership will ensure a high standard of care for those receiving imaging services, while allowing health care systems and medical providers to concentrate on their core businesses

- Carl Armato, President and Chief Executive Officer of Novant Health

“We have known the leadership team at Novant for a number of years and are excited to partner with such a high caliber organization to continue building MedQuest. We believe the company is well-positioned to build its platform in existing markets and establish joint venture partnerships in new markets,

- Zach Ferguson, Managing Director TPG Growth

Strategic Rationale for Novant Health

- Partner with a leading private equity firm to transform and scale an existing asset
- Monetize internally-developed capabilities while maintaining equity and sharing in future upside
- Reinvest proceeds into “core” health system service lines and other revenue diversification strategies
- Position imaging service line for future success amid an increasingly competitive ambulatory services landscape and dynamic regulatory environment

Q&A

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