   

 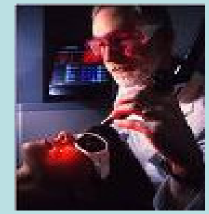

Deciding When to Sell: The Strategy Behind "Holding" or "Folding" and Value Maximization

August, 2008

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Investment Banking

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Table of Contents

West Ridge Associates, LLC

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Management Team

CHARLES TROE,
FOUNDER & MANAGING DIRECTOR

- **More than 35 years of relevant experience**
- **Industry Experience:**
  - **Medical products, technology, telecommunications, basic industry, manufacturing, distribution, banking and finance, insurance, real estate, lodging, and oil and gas**
- **Prior Firms:**
  - **Barrington Associates; Taurus Capital; Mayer Brown LLP; Adams, Duque & Hazeltine; and Andrews & Kurth**
- **Board Membership & Associations:**
  - **Life Science Industry Council, Southern California Biomedical Council, Los Angeles Biomedical Research Institute, Avalon Oil Company, and Hermosa Oil Company**
- **Education:**
  - **BBA, University of Iowa**
  - **JD, University of Chicago**
- **Professional Designations:**
  - **Admitted to State Bar in California, Colorado and Illinois (inactive)**
  - **FINRA Registered Representative (Series 7)**

KAHLIL REID,
MANAGING DIRECTOR

- **More than 10 years of relevant experience**
- **Industry Experience:**
  - **Technology, media, telecommunications, manufacturing, metals and mining**
- **Prior Firms:**
  - **Citigroup Global Corporate and Investment Bank**
  - **Fried, Frank, Harris, Shriver & Jacobson**
  - **Etech Securities, Inc.**
- **Education:**
  - **BS, Cornell University**
  - **JD, Georgetown University**
- **Professional Designations:**
  - **Admitted to the State Bar in New York**
  - **FINRA Registered Representative (Series 7)**
  - **FINRA Registered Securities Principal (Series 24)**

Overview

Overview

- **M&A is the traditional exit for medical technology companies**
  - **IPOs are relatively rare**
    - Markets tend to be smaller
    - Product development times and product life cycles are shorter
    - Product breadth tends to be narrower
  - **IPO Windows come and go – may not match company development stage**
- **JV and licensing deals occur, but not as often as in biotech and pharma**

Overview

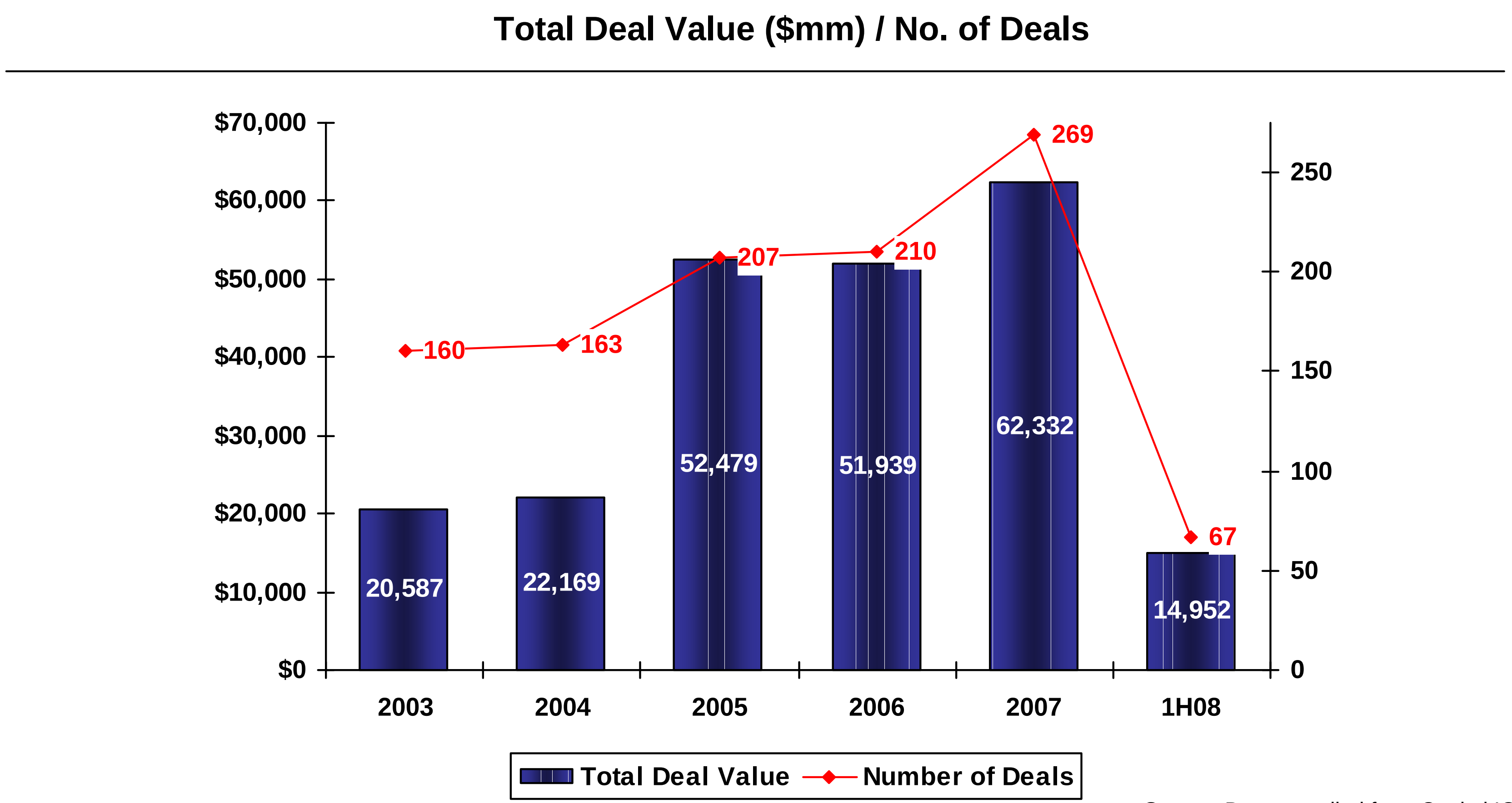
- The Medical Technology industry is driven by distribution
  - There are relatively few very large companies that dominate distribution channels
  - It is difficult for companies with narrow product portfolios to get through the channels
  - The big companies always try to get distribution rights
- Big companies are not always very skilled at innovation
- Small companies are often disadvantaged at manufacturing, sales, and distribution infrastructure.

Overview

- When is it time to consider a sale of your company to maximize value?
  - Good clinical results in the field
  - Market validation of product
  - Further growth would require significant investment
    - i.e., investment in sales and marketing infrastructure or larger manufacturing facilities
  - Hot sector – strike when the iron is hot
    - Cardiovascular, orthopedic, and neurology have had their hot periods
  - Capacity limitations of current management team
  - Investor desire for liquidity
  - R&D capacity limitations may pose obsolescence risk for current product line
  - Potential change in competitive environment such as large company market entry
- Value creation curve

Market Environment

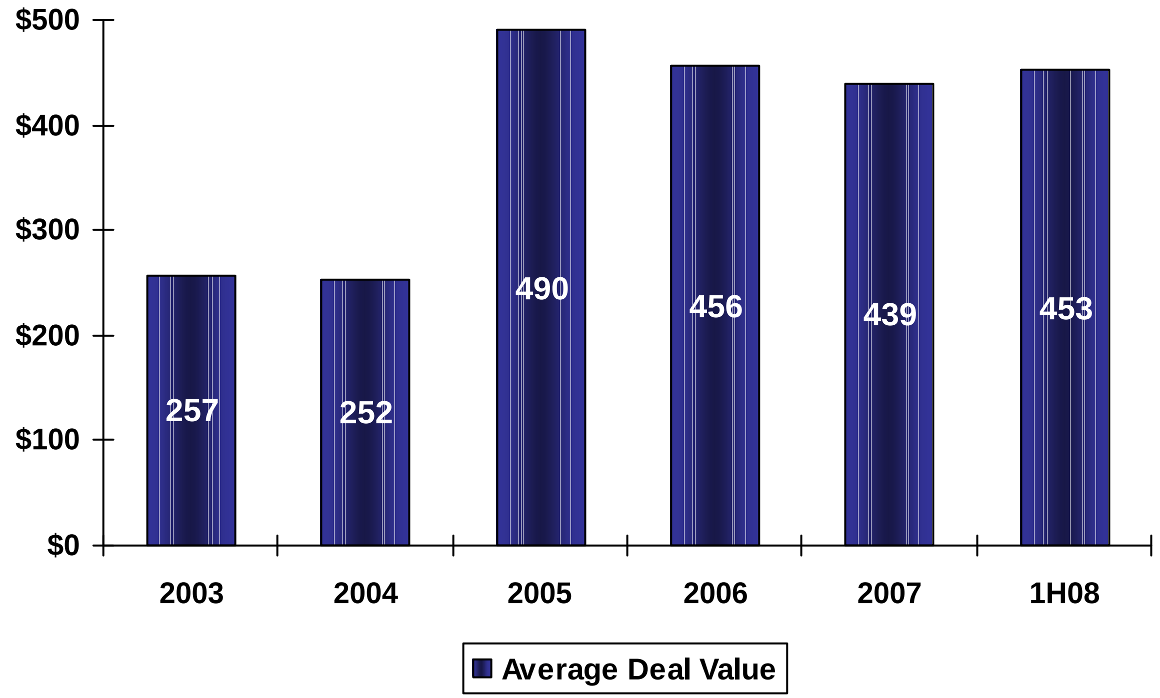
Market Environment – Medical Equipment & Supplies



Source: Data compiled from Capital IQ.

Market Environment – Medical Equipment & Supplies

Average Deal Size ($mm)



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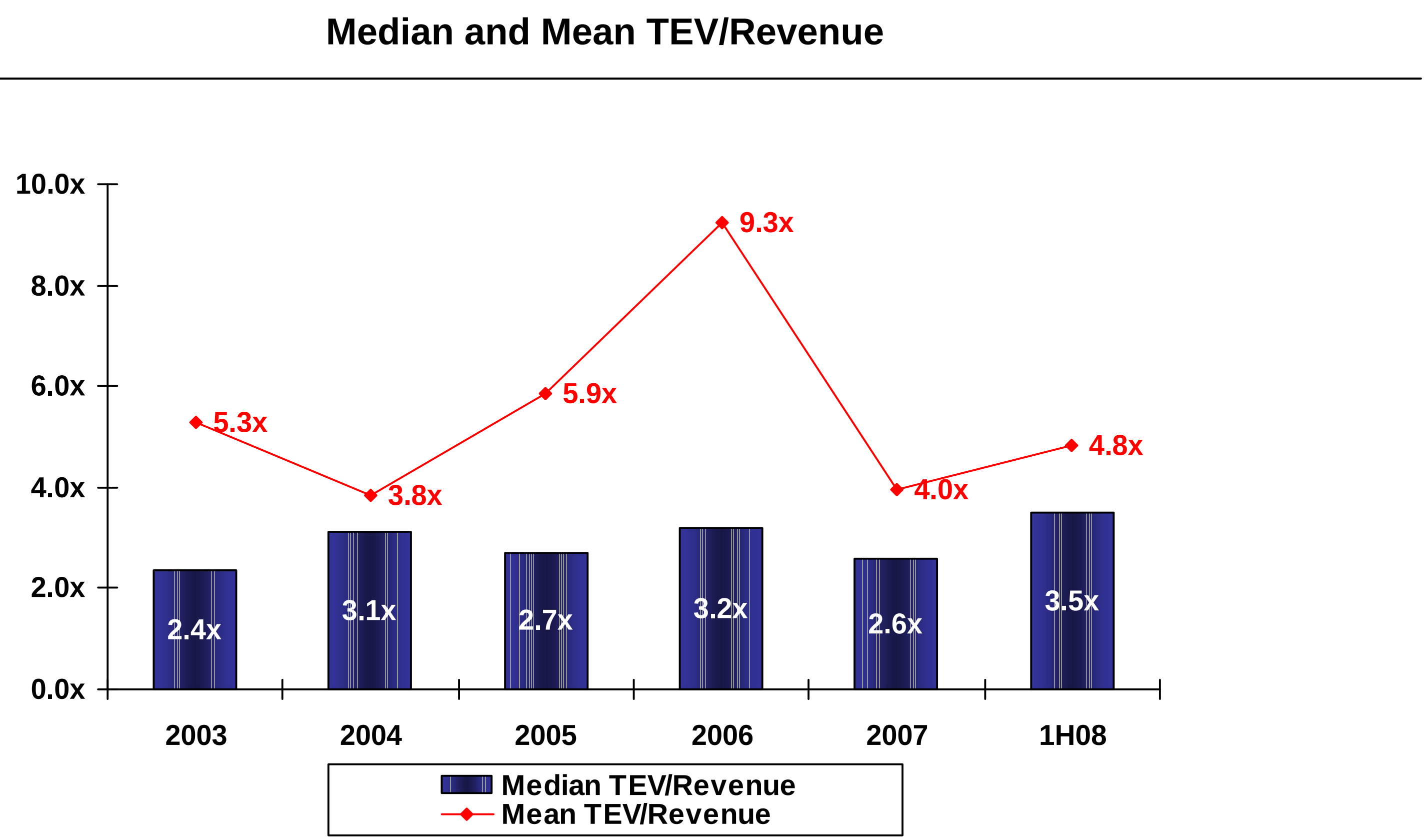
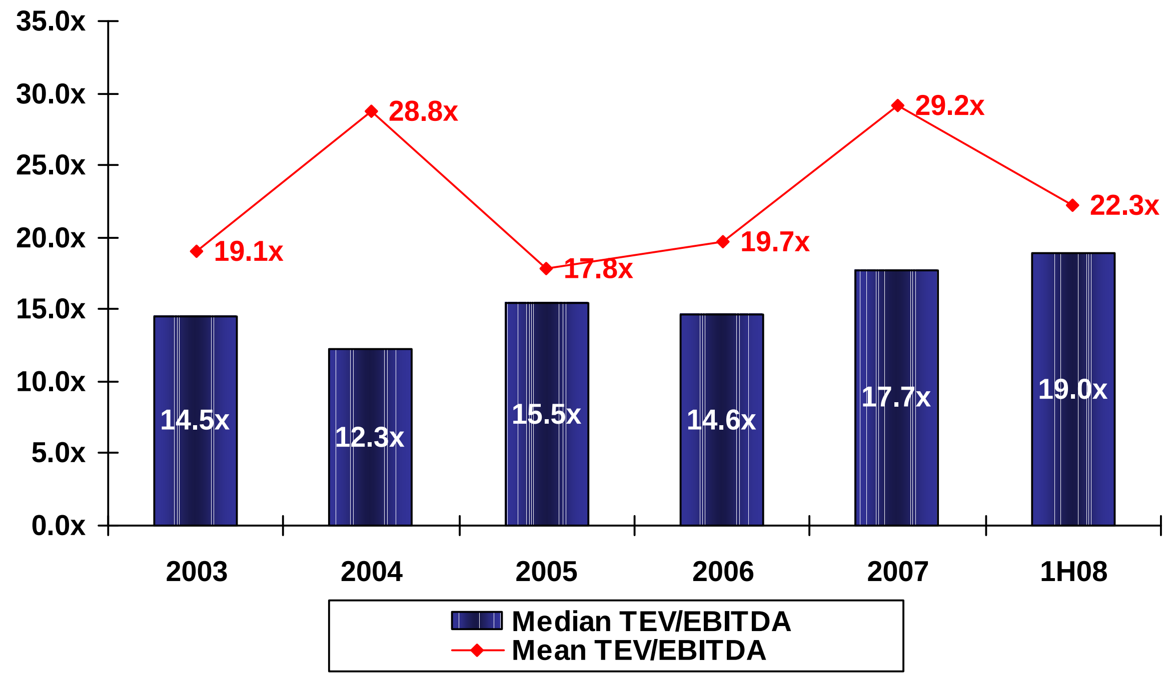
Market Environment – Medical Equipment & Supplies



Source: Data compiled from Capital IQ.

Market Environment – Medical Equipment & Supplies

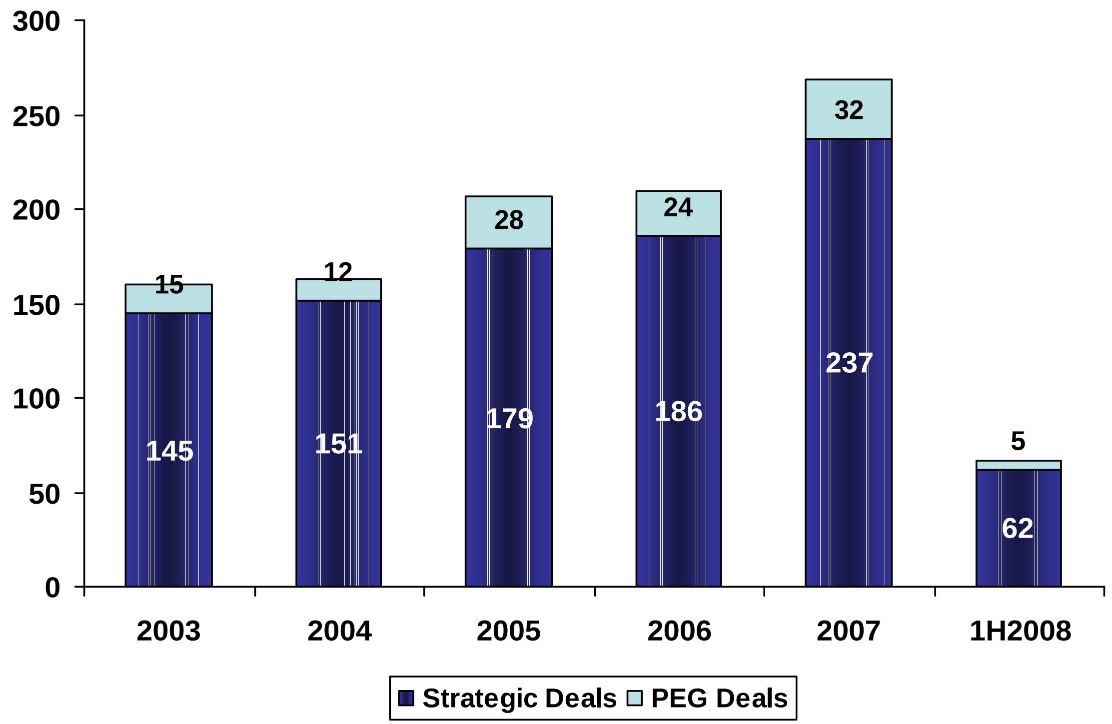
Median and Mean TEV/EBITDA



Source: Data compiled from Capital IQ.

Market Environment – Medical Equipment & Supplies

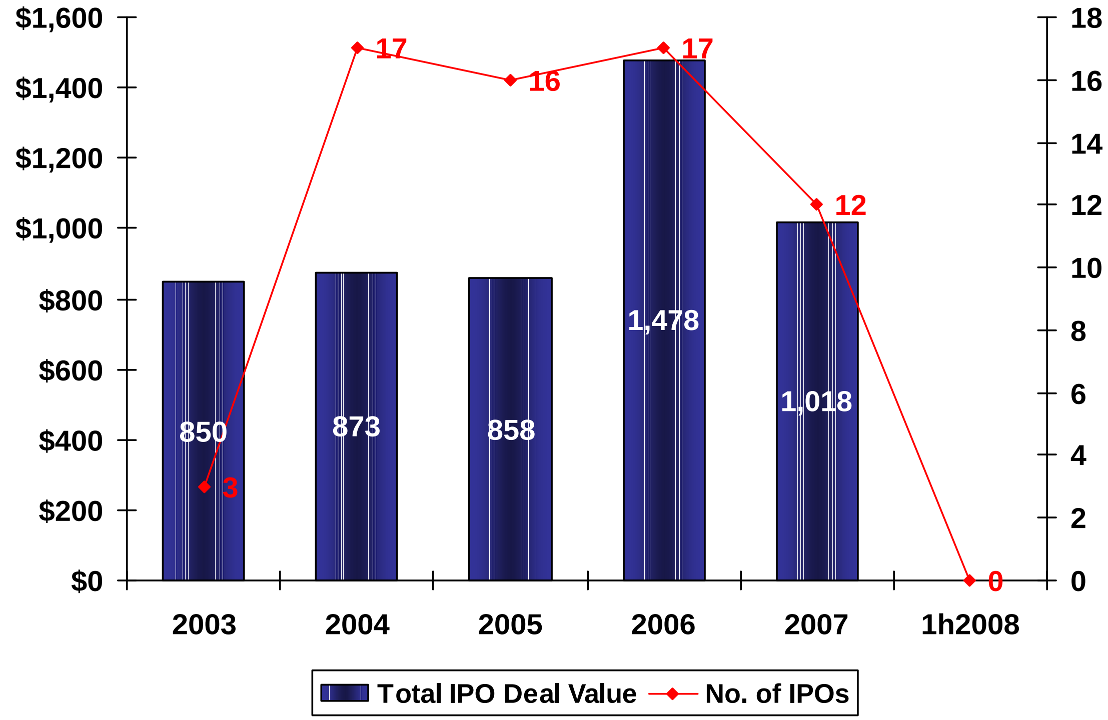
- **Who's Buying?**
  - **Strategic Deals vs. PEG Deals**



Source: Data compiled from Capital IQ.

Market Environment – Medical Equipment & Supplies

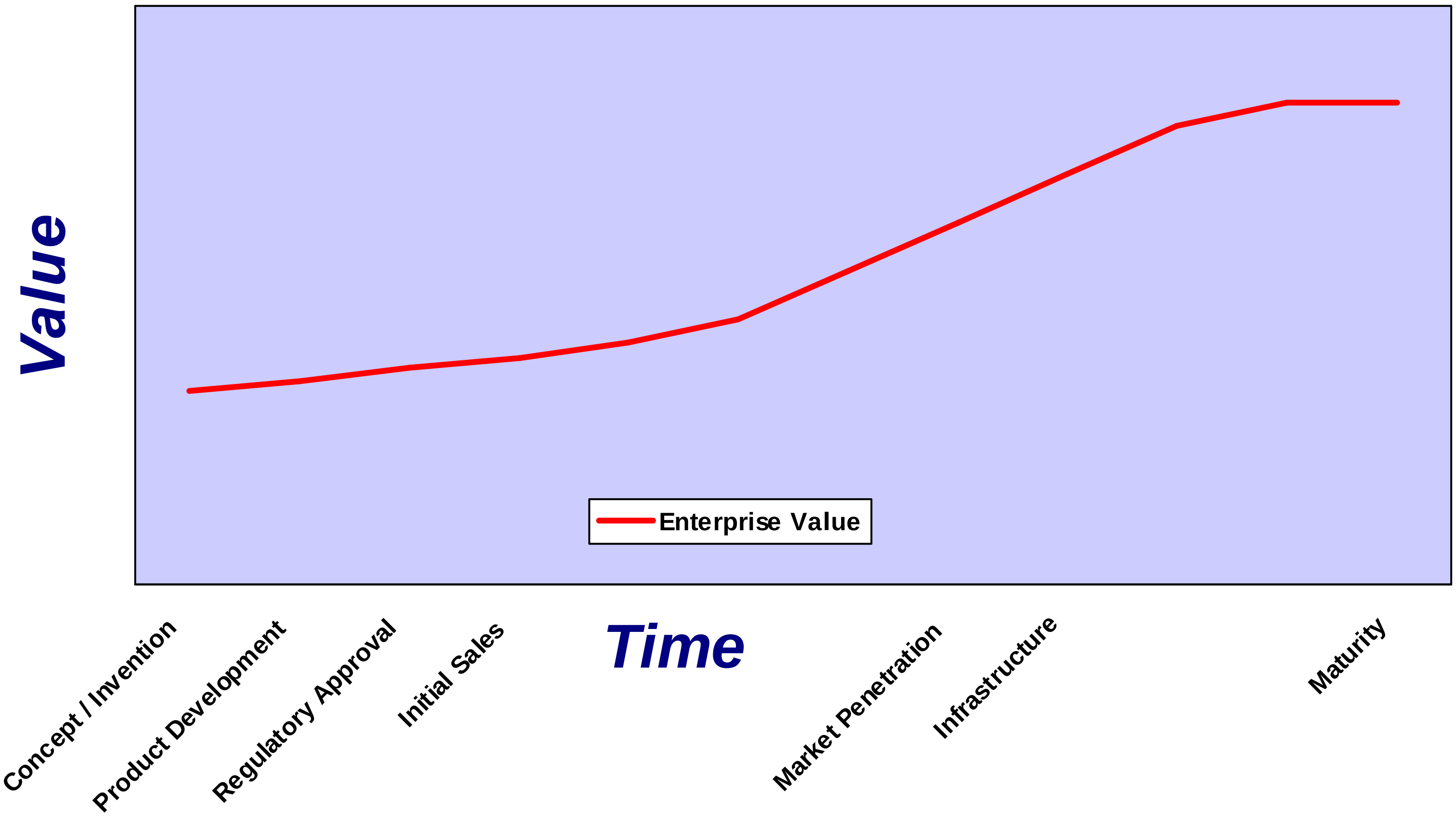
- **Who's Buying?**
  - **IPOs**



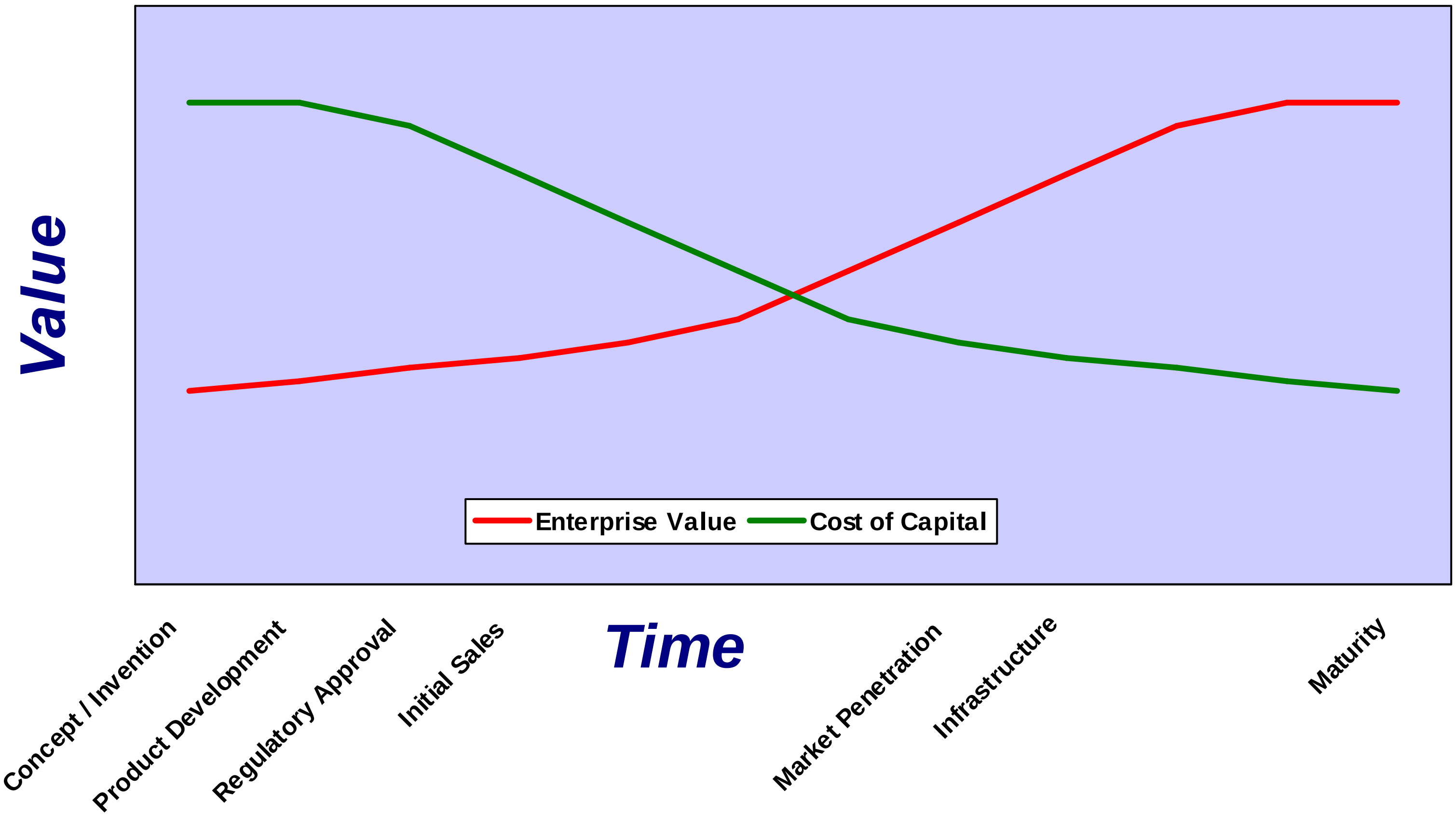
Source: Data compiled from Capital IQ.

When is the Right Time to Sell?

Time/Value Continuum



Time/Value Continuum (cont.)



Strategic Considerations for M&A

- **When does a medical technology company offer the greatest value to a potential buyer?**
  - **Generally, financial buyers will pay only for the financial worth of the target (e.g., the projected free cash flow discounted to present value at a risk adjusted discount rate – or other measure of financial value)**
  - **If the target fits the business strategy, strategic buyers can pay the same financial value,**
    - **<u>Plus</u> the value of synergies created by the business combination resulting, e.g. from existing infrastructure, product extension or complementarity, etc.**
    - **<u>However</u>, the buyer will not want to pay for incremental value that it perceives as being created by attributes, resources or assets it brings to the combined enterprises. . .**
    - **<u>Unless</u> it has to.**

PROCESS DRIVES VALUE

- **Question: Why should I pay you for the incremental value created by putting your product in the hands of a sales force I've spent billions creating?**
- **Answer: Because if you don't, somebody else (i.e., a competitor) will!**
- **Sell Side M&A is the process of extracting from buyers the maximum possible amount of the incremental value created by the combination.**
- **The Process:**
  - **Contemporaneous approach to multiple potential buyers**
  - **For which the acquisition creates incremental strategic value**
  - **Professionally and discretely**
  - **Utilizing high quality materials**

Synergies

Synergies

- **What types of synergies might be derived in a strategic combination?**
  - **Product addition or extension**
  - **Market share increase or elimination of competitor**
  - **Platform technology**
  - **Brand equity**
  - **R&D purchases**
  - **Economies of scale**
  - **Other Cost savings**
  - **Distribution**
  - **Manufacturing capacity**
  - **Management skill**

Synergies

- ***Product Addition or Extension* – merger of firms selling non-competing products to related marketing channels.**
  - **Example: Kinetic Concepts, Inc. acquires LifeCell Corporation (closed May 27, 2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
$1,716.1	8.5x	34.8x

  - **"The acquisition brings together two respected market leaders with well-established best-in-class technologies. This combination allows us to accelerate our strategy to increase KCI's presence in the operating room and will leverage our broad global market reach to drive future growth of LifeCell's products."**
    - **Catherine Burzik, President and CEO of KCI**

Synergies

- ***Market Share* – *Merger of firms selling competing products in the same markets, or separate geographic markets.***
  - **Example: Intuitive Surgical, Inc. acquires Computer Motion, Inc. (closed June 30, 2003)**

TEV ($mm)	TEV/REV	TEV/EBITDA
$51.7	2.1x	NM

  - **Intuitive Surgical's acquisition of Computer Motion, its main competitor, basically gave it a monopoly over minimally invasive surgical robotics. The da Vinci Surgical System is a line of robotic surgical equipment used to conduct cardiac, urological and cancer related minimally-invasive surgeries. While other companies are working on their own versions of systems like the da Vinci, as of the end of 2007, its closest potential competitors are several more years away from releasing their own systems.**
  - **In 2003, the Company acquired its principal competitor Computer Motion, strengthening its intellectual property holdings and ensuring its position as the world's sole provider of robotic-assisted surgical systems.**
    - **Intuitive Surgical website (www.intutivesurgical.com)**

Synergies

- ***Platform Technology Expertise* – *Access to appropriate platform technologies can reduce costs and avoid unnecessary duplication of facilities, increase R&D competitiveness and provide an environment of effective networking and collaboration.***
  - **Example: MEDRAD, Inc. (Bayer AG affiliate), acquires of Possis Medical, Inc. (Closed April 2, 2008).**

TEV ($mm)	TEV/REV	TEV/EBITDA
$319.7	4.3x	95.2x

  - **"The combination of Possis Medical's thrombectomy platform and MEDRAD's vascular injection systems offers a highly complementary focus on high pressure intravascular fluid management and represents a broadened base for future development of new and innovative applications."**
  - **"This merger will capitalize on both companies' strengths to deliver growth in our current markets, and create a formidable cardiovascular portfolio in the future," said John P. Friel, MEDRAD President and CEO. "We welcome Possis Medical as the cornerstone of MEDRAD's cardiovascular strategy…."**
    - **MEDRAD press release dated 2/11/2008**

Synergies

- ***Brand Equity*** ***– Brand equity is the power of the brand to shift the consumer demand curve of a product or service (to achieve a price premium or a market share gain). A buyer may find it more cost effective to buy a brand versus building a brand.***
  - **Example: Medline Industries, Inc. acquires Chester Labs (June 26, 2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
NA	NA	NA

  - **"Chester Labs is a very well-run company with solid, well-recognized brands. This acquisition allows Chester to move more quickly into the development of new technologies that will secure their position as a leader in their field.“**
    - **Andy Mills, President, Medline Industries**

Synergies

- ***R&D Purchases*** ***– There are many different practice areas of medicine, each with separate product lines, therefore it is often cheaper and faster to acquire another company with a rich product pipeline and R&D focus in a specific area.***
  - **Example: Bovie Medical Corporation to acquire the technology, patents and assets from Boston Scientific for RF resection device (announced May 1, 2008).**

TEV ($mm)	TEV/REV	TEV/EBITDA
NA	NA	NA

  - **"This agreement further enhances Bovie's intellectual property portfolio, while creating new significant market opportunities for the company.**
    - **Andrew Makrides, President, Bovie Medical Corporation**

Synergies

- ***Economies of Scale** – More assets and accounts, lower dollar per overhead = greater profits. It's a pretty simple formula, and it usually works.*
  - **Example: Parker Hannifin Corporation acquires HTR Holding Corp. (closed April 4, 2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
NA	NA	NA

  - **Roll up transaction of HTR Holding Corp. group of contract manufacturing companies that sell precision and elastomeric components for medical devices direct to original equipment manufacturers. Provides greater access to medical device market and economies of scale.**
  - **"With our capabilities to engineer innovative, high quality seals in high volume, our combined companies will have increased opportunities to provide value in the life sciences market."**
    - **Heinz Droxner, President of Parker's Seal Group**

Synergies

- ***Cost Savings* – Merger of firms intended to provide cost savings through the integration of the two companies' operations.**
  - **Example: C.R Bard acquires Specialized Health Products International, Inc. (closed June 6, 2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
$59.6	3.2x	16.6x

  - **Special Health Products International was, prior to the deal, an original equipment supplier of winged infusion sets to Bard. This vertical integration provides a cost savings to Bard in that it that it now keeps the margin it once paid to Specialized Health.**

Synergies

- ***Distribution** – Expansion of distribution network through acquisition of new distribution channels.*
  - **Example: Teijn Limited acquires Braden Partners L.P. (pending – announced May 30, 2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
$114.0	0.9x	NM

  - **Braden Partners, which does business under the name Pacific Pulmonary Services, operates more than 100 Patient Care Centers throughout the western United States. It had revenue of $133mm in 2007, placing it among the top 10 in its field. … The move will strengthen Teijin's presence in the U.S. under an ongoing plan of global expansion.**
    - **Teijin press release dated 5/30/2008**

Synergies

- ***Greater Manufacturing Capacity* – *Purchasing additional manufacturing capability versus building.***
  - **Example: NuVasive, Inc. acquires Osteocel Biologics Business from Osiris Therapeutics (July 24,2008)**

TEV ($mm)	TEV/REV	TEV/EBITDA
$85.0	NA	NA

  - **"Our diligence on processing capacity indicates an established and growing supply stream for the product. The transaction is structured to encourage further capacity expansion as we transition this process. Once we have integrated the processing operations, we believe Osteocel will make strong contributions to our revenue growth."**
    - **Alex Lukianov, Chairman and CEO of NuVasive, Inc.**

Synergies

- ***Management Expertise** – Acquisition of firm with specific managerial skill set.*
  - **Example: Arsenal Capital Partners acquired MedicineLodge, Inc. on January 29, 2007. Arsenal Capital Partners merged MedicineLodge, Inc. and Leis Medical, Inc. to form a new company Innovative Medical Device Sourcing (iMDs)**

TEV ($mm)	TEV/REV	TEV/EBITDA
NA	NA	NA

  - **"Our investment strategy is to invest where we have prior industry knowledge and partner with good management teams that can leverage our resources to accelerate growth and business improvement. As we have done in several prior investments, the strategic combination of two businesses has created a more valuable business model with broader and higher value-add services, for their customer base. We will continue to seek ways to grow iMDs organically and through acquisition in order to improve our customer's speed to market."**
    - **James Marden, Managing Director, Arsenal Capital**

Bad Reasons for M&A deals

- **Some bad (i.e., non-strategic) reasons to do M&A transactions:**
  - **Ego – the edifice complex**
  - **Short-term secondary market gain**
  - **Buy-side CEO compensation**
  - **Investment banking fees**
  - **Benefit-benefit analysis**
  - **Amnesia – does anyone remember the conglomeration phase of the 60s?**
  - **Stupidity**
- **One good (i.e., strategic) reason with a bad result**
  - **Incorrect analysis of the strategic consideration**

Going Public?

Don't Go Public Too Soon

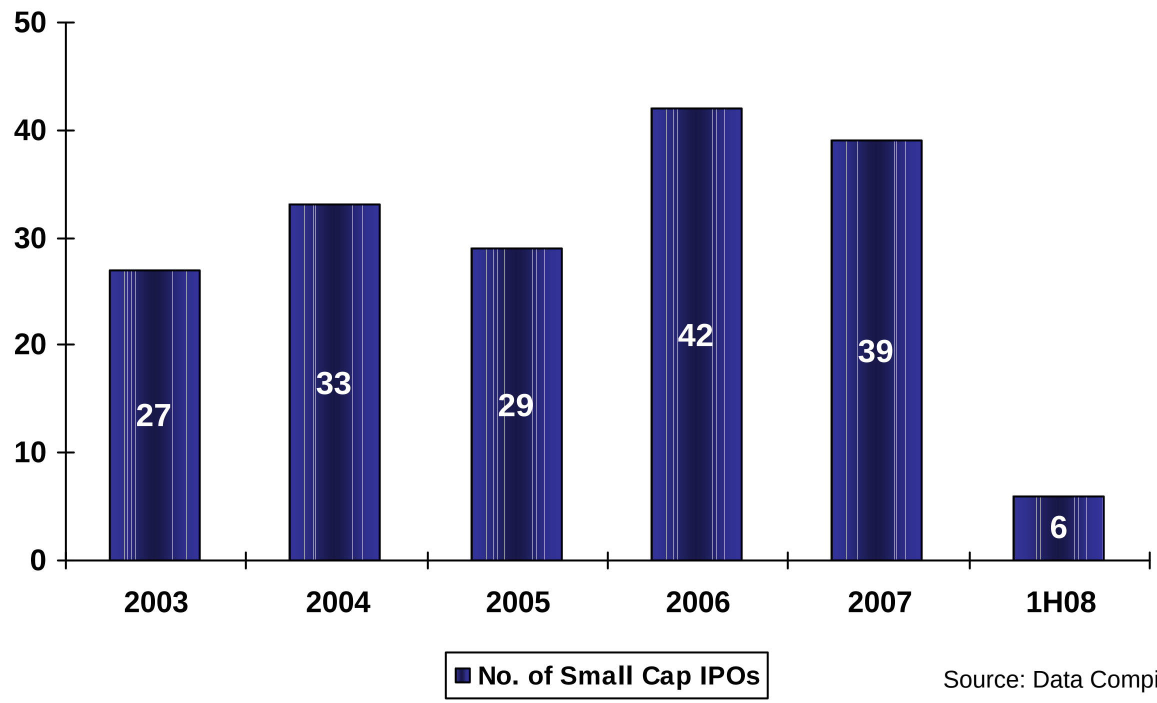
- **Have at least 2 to 3 years of good earnings ahead**
- **Companies should have revenues of about $100 million**
  - **It costs at least $2 million per year to be public (legal and accounting costs)**
    - **Sarbanes-Oxley compliance**
- **Illusory liquidity**
  - **No research = no institutional investors = little or no trading market**
    - **Due to increased regulations after the "dot-com" bust less equity research analyst are covering small cap stocks**
    - **Most institutional investors will only buy stock of companies with research coverage**

Don’t Go Public Too Soon

- **The heightened visibility of public companies allows no room for missteps**
  - **Missed earnings**
  - **Accounting irregularities**
  - **Executive scandals**
  - **Product defects/recalls**

IPO Market Recap

Total U.S. Small Cap. ($1mm-$20mm) IPOs



Source: Data Compiled from Capital IQ

Q & A