HM GOES PUBLIC

IPC blazes trail with stock offering

By Marlene Piturro, PhD, MBA

Adam Singer, CEO of IPC, signals the start of trading at the Nasdaq in New York City.

You know your industry is on the map when a trailblazer takes his company public. That signals the capital markets that top executives in a leading company are confident in their business model's ability to grow the company enough to satisfy Wall Street's voracious hunger for profits.

It's a tall order, and Adam Singer, MD, founder and CEO of IPC-The Hospitalist Company, based in North Hollywood, Calif., accomplished it in January.

During 2007, Dr. Singer set the wheels in motion for taking IPC public the following year. "Our company is built right, has a solid revenue stream, and the nirvana of a real healthcare company—a battle-tested, proven business model," he says.

Dr. Singer and his management team had the usual reasons for going public: raising capital to pay for operations and to allow for growth by acquisition, reducing debt, and creating liquidity for shareholders. He also had other fish to fry with a public offering. "I wanted to be the first in our industry to make it out of the box," he says. "I also wanted IPC to be a model for the many hospital medicine companies that would like to mature beyond having a bunch of doctors running around a hospital and calling themselves a hospitalist medicine company."

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For Dr. Singer, going public went beyond the desire to produce quarterly financial results that would warm investors' hearts. It spoke to his core belief in what the business of hospital medicine should be and, from his vantage point, isn't.

"By leading a publicly traded hospital medicine company I am debunking the myth that hospitalist groups need hospital subsidies to survive," he says. "This is a powerful myth, one that is mired in a work force's idea that its members should get full-time pay for less than full-time work. IPC has raised the bar for our industry. We think that hospitals should demand the overall level of sophistication, physician commitment and productivity that IPC has."

With few publicly traded physician companies for templates for a public offering, Dr. Singer looked to a colleague, Roger Medel, MD, for direction. Dr. Medel took his company public in 1979 and has grown Sunrise, Fla.-based Pediatrix Medical Group, a provider of neonatal, maternal-fetal, and pediatric intensivist/hospitalist services, from a company with $100 million in market capitalization to $3.32 billion and a recent stock price of $67 per share. The company has a "buy" consensus rating from analysts and respectable price-to-earning and earnings-per-share values.

Economic Evolution

Medical staffing firm IPOs, such as IPC's, are relatively rare. Most venture capital chases the next hot thing in medical information technology, biotechnology, and medical testing. The quirks of the medical staffing industry, such as hospitalist hiring—where salary increases can consume sizable chunks of a firm's revenues—may deter potential investors.

Why are publicly traded medical staffing companies like IPC and PDX the exception rather than the rule? Because they rely so heavily on human capital—primarily physicians—for bottom-line results, they must contend with recruiting and retaining from a highly sought after talent pool that have their choice of job opportunities.

Also, many physicians fear the corporatization of medicine, an anxiety that working for a publicly traded company tends to arouse. Physician idealism—wanting to make the world a better place—may clash with a public corporation's raison d'etre: making money. In a young field like hospital medicine, where performance metrics are evolving, balancing shareholder demands for ROI versus quality patient care requires a delicate touch.

Larry Wellikson, MD, SHM's chief executive officer, says IPC's entry into the public markets has been received well, indicating the maturation and strong growth of hospital medicine.

IPC's public offering took place Jan. 30. Lead underwriters Credit Suisse Securities and Jeffries & Co. offered 5.9 million shares of IPC stock under the ticker symbol IPCM, a four-letter symbol conforming with NASDAQ's listing requirements. The stock traded mostly at $19 per share, above the original per share estimate of between $15 to $17, raising approximately $38.3 million in net proceeds.

Since then, IPCM shares have ranged from $16.25 to $23.09 per share, trading at a thin average daily volume of 162,000. As of March 31, IPC's market capitalization was $296 million. Six months from the IPO, average daily volume should increase, as regulations on shareholder sales are eased according to stock exchange rules.

IPC's latest financial results were upbeat. The firm reported record operating results for the fourth quarter and full year 2007. Total patient encounters rose 29%, compared with 460,000 over the same period in 2006. Fourth-quarter net revenues were $52.6 million, a 31% increase from $40.2 million in fourth-quarter 2006. Physician practice salaries and other expenses for the period were $36.9 million vs. $29.5 million for fourth-quarter 2006. As a percentage of net revenue, physician salaries declined to 70% from 73% in the fourth quarter of 2007 vs. 2006. Dr. Singer attributed the change to higher physician productivity and increased revenue per encounter.

With the stock market retrenching since its all-time high in October, IPC's timing on going public might seem a bit off. Yet, venture capitalists are bullish on healthcare. They sank a record $9.97 billion into the sector in 2007, topping the previous high of $9.47 billion in 2000, during the dot.com craze. Three large venture capital firms specializing in healthcare have $1.25 billion looking for good homes. The worry on Wall Street is that there won't be enough healthcare IPOs to satisfy demand; there were only 31 in 2007 vs. 60 in 2000.

Alternatives

Going public is not the only way hospital medicine companies and other physician-intensive enterprises can raise needed capital. Venture capital plays a critical role. Brentwood, Tenn.-based Cogent Healthcare received its first round of such funding in 1997, a second infusion in 2000, and $15 million in 2002. IPC is no stranger to venture capital either: It raised $47 million in venture capital since 1998. Such capital infusions helped IPC and Cogent in their early days by providing the money needed to start hospital medicine groups, recruit top managers, expand into new markets, and improve IT and communication infrastructures.

Some entrepreneurs favor keeping their companies private. For example, John Erickson, founder and CEO of Baltimore-based Erickson Retirement Communities (ERC), is committed to growing his business without going public. There are 19 Erickson campuses in 11 states, with 21,000 residents. ERC's business plan involves adding sites, anticipating growth to 55,000 residents in five years. Such steady expansion gobbles up capital, but Erickson is adamant about staying private. On going public he says: "I consider it whenever I need capital, but it's hard to keep public markets happy. If your business slows down for any reason, your stock tanks and the market will punish you harshly. I will not have stock analysts pressuring me about how to run and grow my business."

Erickson admits the competing demands of raising capital and keeping the company private aren't easy to reconcile. "We go to midsized and large banks and [real estate investment trusts], get letters of credit, tax bonds, debt financing, mezzanine financing, etc.," he says. He considers that others in his industry, Sunrise Senior Living (SRZ) and Brookdale Senior Living (BKD) that have gone public show the industry's strength. "Multiple sources of capitalization in an industry provide greater options for all," he adds.

That said, Erickson intends to resist any temptation to go public because "I must have the flexibility to implement our five-year plan correctly. If I want to invest $30 million in a medical group or hire seven doctors at $150,000 a pop, I don't have to answer to some 30-year-old stock analyst who doesn't like that."

As for IPC's public offering, Erickson says the first company to do so in an industry opens new avenues for raising capital in the public arena. "Dr. Singer's pushing the envelope for hospital medicine, and if he can tolerate the pressure of the market—even when the strings are very tight—that's great," he emphasizes.

Commenting on the legal and governance issues of a public offering, Peter Olberg, corporate and finance partner at Manhattan-based law firm of Manatt, Philips and Philips says IPC's being the first publicly traded hospitalist medicine company is a sound way to raise capital and isn't risky in terms of disclosure. However, a specialty care provider like IPC can "become a victim of its own success. Public payers can say reimbursement

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TIMELINE OF IPC'S INITIAL PUBLIC OFFERING

Prior to its 2008 IPO, IPC's largest institutional backers/owners were Bank of America Ventures, 30.92%; Morganthaler, 25.13%; Bessemer, 17.38%; and CB Health Ventures, 14.80%.

- **1988-2007:** $47 million in venture capital invested since 1988.
- **2007:** Credit Suisse Securities and Jeffries & Co selected as joint underwriters; Wachovia Capital Market and William Blair & Co as IPO co-managers.
- **August 2007:** IPC plans a 2008 IPO to sell $105 million of common stock; 2.8 million shares in the IPO, 1.9 million by shareholders.
- **Jan. 20:** IPC released financial highlights on net revenues and net income. IPO planned of 4.7 million shares at $15 to $17 per share; net proceeds of approximately $38.3 million anticipated.
- **Jan. 30:** IPO of 5.905 million shares.
- **Feb. 11:** IPCM makes its first acquisition as a publicly traded company by purchasing Ludlow, Mass.-based Innovative Physician Services, 38 hospitalists group caring for 300 patients daily, in 12 acute care facilities. *—MP*

MARKET ENTRY SPURS CURIOSITY AND CONCERNS

As chief of a 25-physician hospital medicine group at Philadelphia's Temple University Hospital, which is run by Cogent Healthcare, IPC's public offering is of great interest to William Ford, MD.

"I am thrilled that people smarter than me have decided that hospital medicine is a solid investment," says Dr. Ford, a Cogent medical director. "Going public was a good thing for IPC and a fantastic thing for hospital medicine. It shows our specialty has a business model that can sustain growth and that IPC has a platform on which a hospitalist company can build successfully.

"The problems with going public are daily scrutiny by the market and the media and the need to satisfy investors' primary goal, which is making money," he continues. What remains to be seen is if IPC can balance stockholder thirst for returns and the company's performance long term.

Dr. Ford won't comment on Cogent's prospects for going public but says Cogent's business model, which includes hospitals supporting their hospital medicine programs, also is sound. He points out that Cogent partners with its hospitals to reduce variations in care, develop best practices, and remove barriers to efficiency.

Elaborating on such funding, which IPC eschews, Dr. Ford adds that while the "2005-2006 SHM Survey: State of the Hospital Medicine Movement" shows that hospital support averages $75,000 to $120,000 per physician annually, the numbers show that the efficiencies hospitalists deliver outweigh the cost of such support.

Another issue hospital medicine detractors raise is that hospitalists haven't dramatically cut costs, so their support is unwarranted.

However, a 2007 *New England Journal of Medicine* article documented that hospitalists reduce costs modestly: $125 for reduced length of stay and $268 in lower costs per case.[1]

Dr. Ford goes so far as to say drops in payer reimbursement wouldn't jeopardize hospitalist medicine's existence. "Even if Medicare cut reimbursement to zero, hospitals will stay open and they'll need hospitalists to care for patients," he asserts.

One potential flashpoint for a publicly traded hospitalist company is patient volume. "Wall Street may want me to see 25 to 30 patients a day to drive revenues—an eat-what-you-kill mentality. On an average day a hospitalist in my group sees 14 or 15 patients. That works well in avoiding burnout and reducing the average $75,000 it costs to recruit a new physician," he says.*—MP*

REFERENCE

1. Lindenauer PK, Rothberg MB, Pekow PS, Kenwood C, Benjamin, EM, Auerbach AD. Outcomes of care by hospitalists, general internists, and family physicians. *N Engl J Med.* 2007 Dec. 20;357(25):2589-2600.

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is too high and cut it based on the leader's financial performance."

Peer Perspective

SHM President Patrick Cawley, MD, MBA, calls IPC's public offering a major milestone because it demonstrates the maturity of the hospitalist movement. He expects IPC to use the infusion of capital to step up physician hiring, acquire more groups, and improve its proprietary IT infrastructure by refining its tools to further link outcomes and performance.

"IPC's emphasis on quality outcomes is clearly where medicine is going," Dr. Cawley says. And, "Putting pressure on hospitalists to be more productive has a huge potential in helping hospital medicine get more efficient by seeing more patients."

To put the IPC public offering in perspective Dr. Cawley captures Dr. Singer's vision. "To run a public company, you focus beyond daily stock prices and on the intermediate and short-term. What Wall Street thinks about your business matters. Our product [hospital medicine] has a great future, and I applaud Adam Singer for taking this step."

Giving Dr. Singer the last word, he says "I'm a big believer in not worrying about things I can't control like stock market fluctuations. We can handle good news and bad. We have a good business model and we'll stick to the knitting." TH

Marlene Piturro is a medical writer based in New York.

PRESCRIPTION FOR A SUCCESSFUL IPO

- Have a foundation of 10 years of business mentoring and venture capital;
- Have a business that is completely "baked";
- Make sure your business model moves the needle on performance;
- Feasibility in planned growth and reliable in performance measures;
- Have robust IT infrastructure; and
- Develop a top notch management team and guard against a "weakest link."