

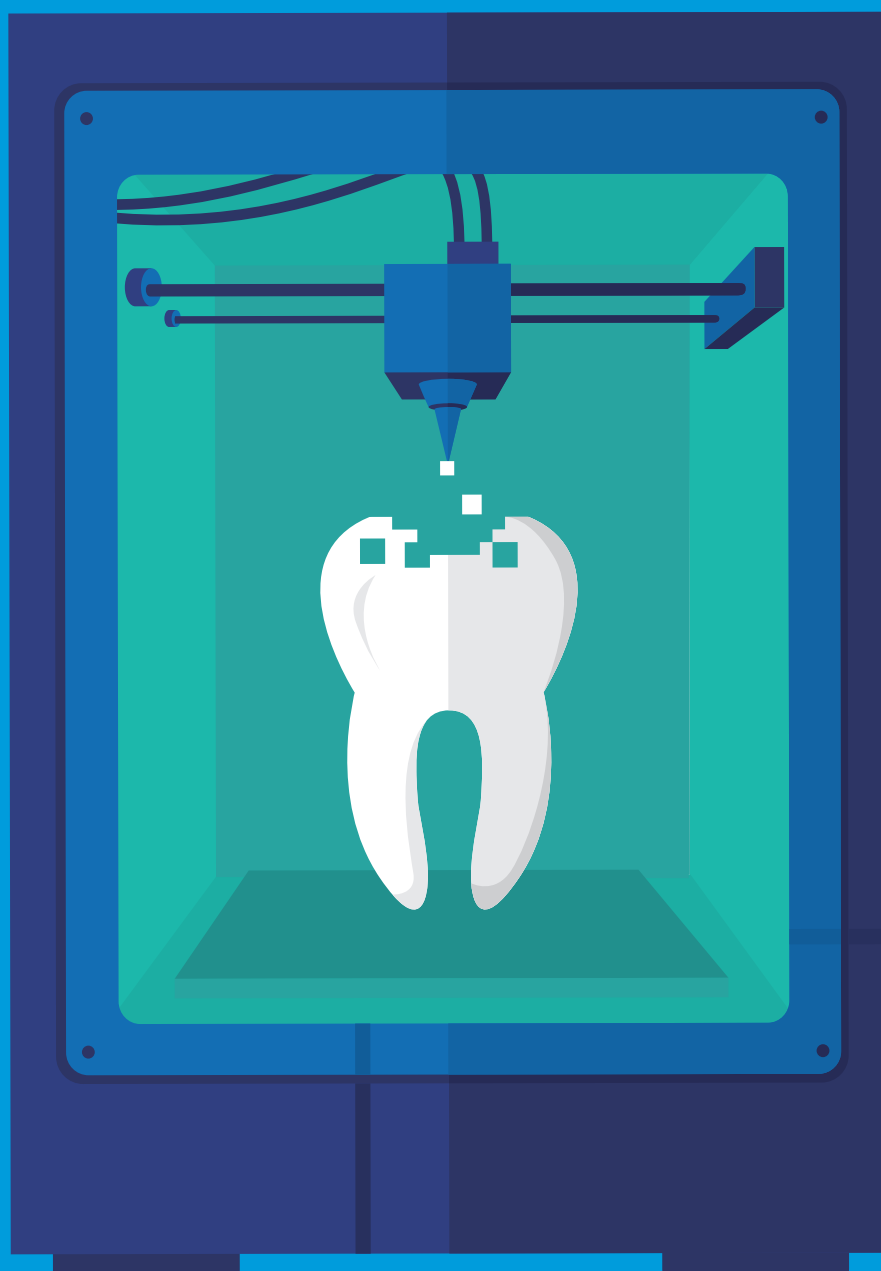


The dental chain opportunity

Consolidation of the European dental industry is in its early stages

Realising value series

Despite the growing liberalisation of healthcare markets, the dental sector in Western Europe, including Ireland, remains highly fragmented and presents a significant investment opportunity for private equity firms and strategic buyers from adjacent healthcare sectors. Consolidation and the creation of dental chains can bring significant operational and procurement efficiencies, as long as local market differences and customs are respected.



Consolidation of the European dental industry is in its early stages

To date, relatively few chains of practices have made an impact on the European dental market, estimated at more than US\$70 billion. Private equity houses are starting to see the potential and are already active in this space, buying individual practices and groups to form larger chains. There remains exciting potential.

In addition to stable or growing demand in most parts of the region, investors are attracted by the possibility of achieving scale economies through shared services, a shared talent pool and the option to vertically integrate into laboratories and other services.

But in building a pan-European operating model, chains should be wary of becoming faceless corporate organisations that lose the personal touch that is so important to patients. A strong local management team, with a focus on long-term profitability over quick wins is important. This helps to ensure that customer intimacy and quality of care is maintained and that the business adapts efficiently to country specific regulations and market requirements.

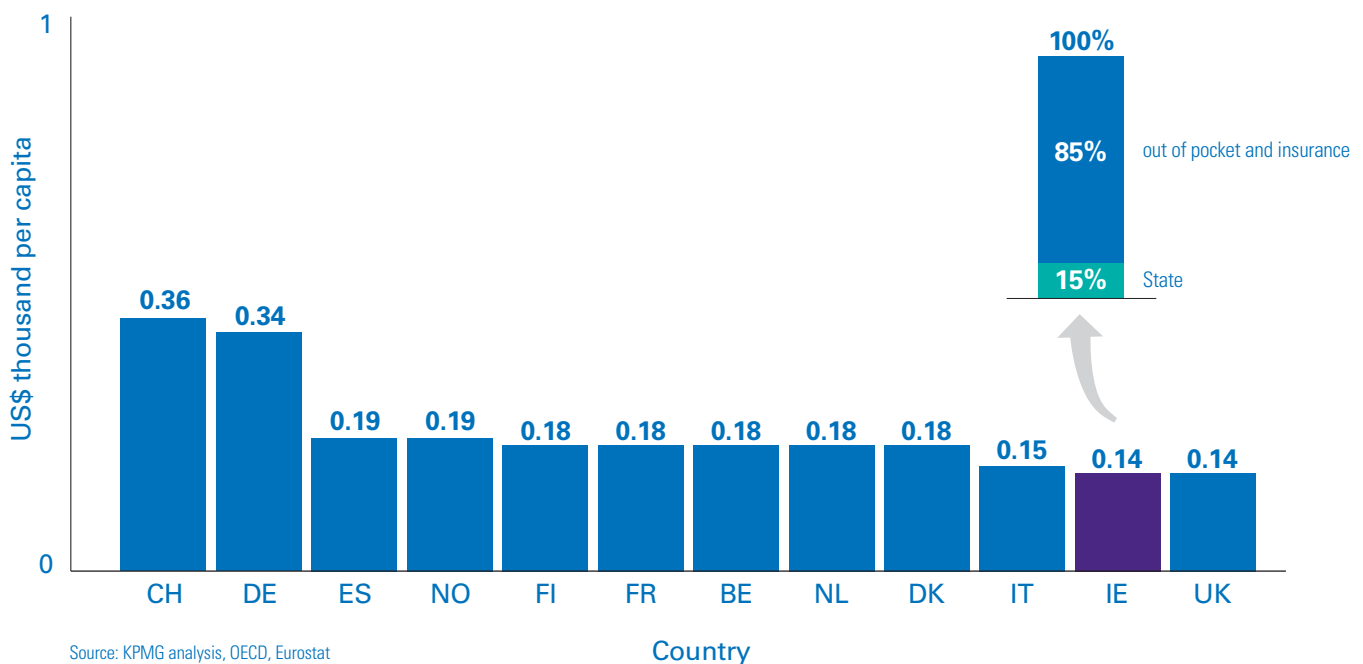
To better understand the scale and nature of this investment opportunity, in late 2016 KPMG surveyed more than 100 dental experts from the Netherlands, Germany, UK, Sweden, Denmark, Italy and Finland. Our research involved structured telephone interviews with dentists, practice owners, heads of dental associations and healthcare insurers and, together with our project experience in this space, has informed the basis of this article. This has been added to by the local Irish team.

High potential in a fragmented market

Following the introduction of partial free market activity in healthcare over the past decade or so, a number of governments across Western Europe are aiming to counter the dual challenge of rising demand and budgetary restrictions, by stimulating higher levels of efficiency and quality. Although this liberalisation has helped drive increased merger and acquisition activity

in other healthcare industries like hospitals, care centers and private clinics, consolidation in the dental care industry remains relatively low. Yet the size of the Western European dental sector (estimated at more than US\$70 billion) and high levels of fragmentation, suggest an industry ripe for consolidation. This is a picture mirrored in Ireland.

Dental care market by country (in customer spend), 2015 – 2017



Dental markets in most European countries are generally dominated by small practices, on average consisting of one to three dentists.

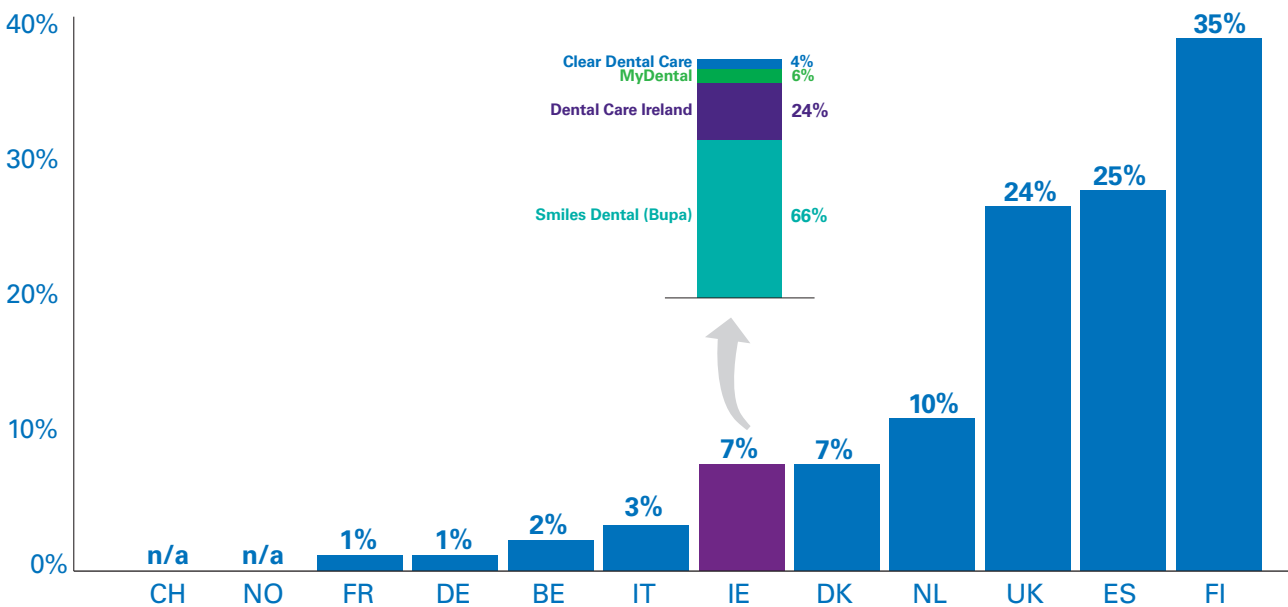
Aside from the cost challenge associated with operating as a small business, the current small practice model is already under pressure, with many dentists approaching retirement age, a lack of newly qualified professionals to replace them, and a substantial number of younger (often female) dentists preferring to work part-time and therefore reluctant to own their own practices. According to one of the European dentists taking part in our survey, “solo-practices have a very hard time and will vanish eventually.”

This creates a sizable opportunity for private equity and strategic investors – like private healthcare providers already operating in adjacent sectors – to buy individual practices and groups and create chains to introduce scale economies, efficiencies, and better manage risks such as business continuity at retirement. A number

of our interviewees echoed this sentiment, with one commenting that “older dentists are very willing to sell their practice to a chain. They see it as a perfect solution to continue working at the end of their career, while avoiding the administrative burden of having your own practice.”

Consolidation has been most pronounced in Finland, where chains account for 35 percent of the market (in terms of number of dentists). Ireland is more fragmented, but with at least two chains actively seeking expansion opportunities. Of the larger nations, only UK and Spain have a significant proportion of chains – and these represent just one quarter of the total. Germany may be the biggest dental market in Western Europe by size, but 99 percent of its practices are small.

Market share of dental chains (in number of dentists)



Note: Irish dental chain breakdown from identified players in 2017, other figures as of 2015.
Source: KPMG analysis, OECD, Eurostat

Market demand is fundamentally stable

In terms of growth, Western European dental markets have been relatively stable in recent years, with most expected to either remain at current levels or grow by a few percent annually.

Where growth is anticipated, this is driven by rising populations, aging (which often brings a range of more complex dental problems), an increased desire to preserve one's own natural teeth, and a rising demand for preventive care due to awareness of oral hygiene, as part of a wider shift from 'cure' to 'care.'

Despite dental visits in the struggling economies of Spain and Italy falling in recent years, the overall prospects for Europe appear sound, with dental care widely considered a necessity in the majority of countries. In the Netherlands, for example, some 75 percent of citizens visit their dentist at least once a year, with similar figures in the Nordic countries. By contrast, it is estimated that a mere 40 percent of Spaniards see their dentists annually, although such numbers could also be viewed as an opportunity to expand the market through communicating the need for dental health – especially as dental care is, arguably, affordable in both Spain and Italy.

In Ireland, the economic downturn did see a drop in both private spend and public funding, but the sector is now in rebound.

Across the region, funding for dental care varies. In some nations the cost of care is covered partly or wholly through public healthcare insurance schemes, whilst in others, patients must pay supplementary public or private insurance, or alternatively pay directly for treatments. At the time of writing, no major changes to insurance policies are expected in the near future, and as a result the dental market should remain reasonably buoyant.

The attractiveness of a particular market is also heavily influenced by the stability of its healthcare system. Private equity investors are more likely to be interested in creating chains in a country where future conditions are mostly predictable. Italy is currently undergoing a number of reforms and innovations, the impacts of which are difficult to assess (in terms of payment

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procedures and prices to patients), as laws are yet to be fully implemented. The impact of recent major healthcare reforms on dentists in Finland also remains unclear. With the exception of these countries, there do not appear to be any major planned regulatory reforms likely to impact dental markets. Even price rises typically tend to produce a modest temporary fall in demand, which is often soon reversed, and hence not considered to be a major deterrent to investment decisions.

The trend towards subscription-based pricing for private dental care – as evidenced in Finland and the UK – could shift the balance of power from insurers/payers to the dental practices, in the process creating a more positive environment for investors, who can count on an even more reliable revenue stream. Subscriptions are also good news for the payers, leading to timely and preventative dental treatments and improved oral care.

Increasing merger and acquisition activity

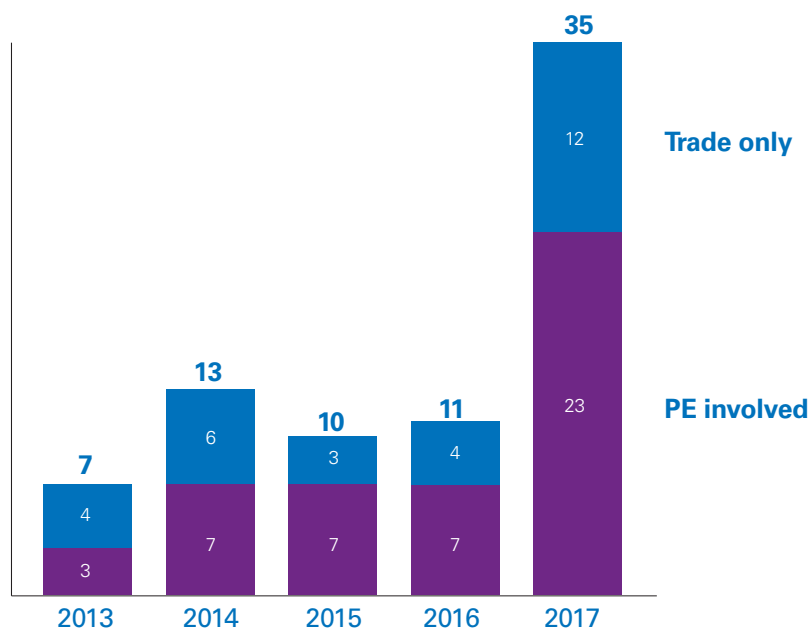
The potential in the European dental market has not gone unnoticed, with a steady flow of deals in several countries, much of it initiated by private equity players. The Carlyle Group and Palamon Capital Partners jointly own the UK's largest dental chain, mydentist, which was formed in 2011 and now operates over 650 practices. In 2013 Bridgepoint bought the number two chain, Oasis Healthcare, and sold it again in 2016 to private healthcare insurer Bupa. Bupa, which has owned a stake in Spanish healthcare and dental chain Sanitas since 2003, initially entered the UK dental market in 2014 when it bought Barbican Dental Care. But the acquisition of Oasis has catapulted Bupa into the leading ranks of UK dental care providers, with more than 400 practices and over 2 million customers. Such a move could potentially signal the entry into the market by other strategic investors from adjacent healthcare sectors.

In the Netherlands, leading dental groups Samenwerkende Tandartsen and Tandartsen and Tandvitaal have been majority owned by private equity firms, NPM Capital and Bencis Capital Partners respectively, since 2011.

Ireland has seen investment both from Bupa (in Smiles Dental) and private equity. Private equity houses are also active in the Nordic dental markets, with interests in both Colosseum Dental (since 2010) and Oral and Med Group. Similarly in Southern Europe, Italy's DentalPro, the country's biggest chain, has been controlled by Summit Partners since 2015, and Spanish/Italian chain Vitaldent is partly owned by Spanish private equity firm JB Capital.

Despite these developments, consolidation is still at an early stage in most parts of the region, with the possibility of exciting rewards for investors able to successfully gain operational and vertical integration efficiencies.

M&A volumes in the European dental industry



Source: KPMG analysis, OECD, Eurostat

Creating a pan-European dental operating model

Our discussions with market experts reveal a host of benefits offered by larger chains. Back-office functions like Finance, IT, Procurement, Marketing and general management can be centralised in a shared service center, reducing overhead costs and enabling procurement discounts on disposables, instruments and equipment (which make up a high proportion of operating expenses). Shared service centers are common in most current chains, freeing up existing dentists to focus on providing care to patients. Once a dental chain has achieved scale, it also has the financial clout to negotiate better rates on property leaseholds.

A wide, local talent pool of dentists, specialists (like hygienists) and support staff, spread across multiple practices, enables the company to allocate work across different practices during times of high demand. This should increase overall capacity and minimise the chance of turning down patients. With more staff to choose from, and with larger facilities in high-

traffic areas like shopping malls, practices could open in the evenings and even weekends, further increasing volume. A sizeable chain, with a renowned brand, is also more likely to attract dentists and other staff, and overcome skill shortages.

Most of today's smaller practices rely on third-party technical laboratories to produce crowns and implants. The increased resources of a chain allow vertical integration into centralised dental laboratories that serve all the practices. mydentist, one of the UK's largest chains, claims to be the largest integrated dental services business in the country, and operates its own labs. By producing crowns, implants and bridges in-house at lower cost, a chain can improve its profitability and even gain additional revenues by selling outside the business to other practices. Dental chains could even boost margins by locating laboratory work in low-wage countries such as China, Taiwan or Eastern Europe – being careful to ensure that technical quality is not compromised.

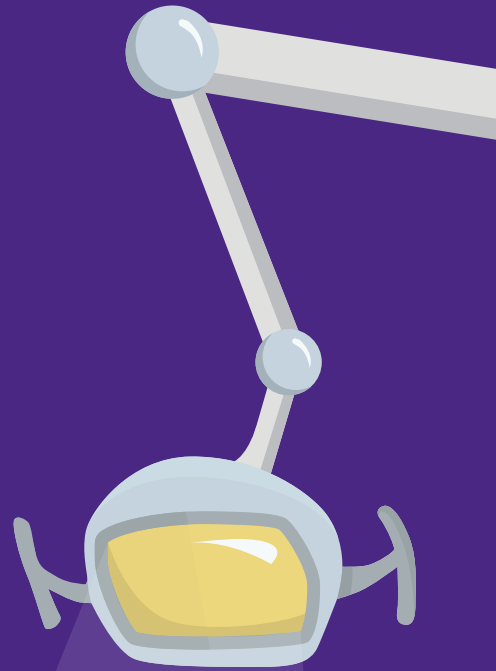
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Dental chains are also well-positioned to take advantage of technological developments like computer-aided design and computer-aided manufacturing (CAD/CAM) and 3D printing, which are less labor intensive and can shorten supply chains for – and reduce the cost of – crowns and bridges. Smaller practices may be hesitant to invest the large sums needed to buy such equipment, which could put them at a disadvantage when it comes to attracting patients who prefer high-tech dental surgeries. The investment in technology could, over the longer term, be a pre-requisite for attracting and retaining patients and hence act as an additional factor driving consolidation.

One of the dentists we interviewed was keen to highlight the importance of vertical integration and technology investment from a customer satisfaction perspective, noting that “a chain often has a lot of specialisations, which means the patient does not have to go somewhere else to get a certain treatment.”

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Similarly another survey participant – a member of a patients’ association in Europe – was equally upbeat about the trend towards chains: “The appearance of chains is positive for the dental industry. It will result in more professionalism, better services and quality for patients.”



Benefits of consolidation

	Investors/owners	Patients	Regulators/government	Payers/funding
Quality	<ul style="list-style-type: none"> • Strong brand generates a recurring customer/revenue base • Patients trust their dentist and feel comfortable with more complex treatments • Wider disciplines providing full-scope care 	<ul style="list-style-type: none"> • Consistent quality levels for preventive and restorative treatments • Larger practices allow for dentist specialisation and provision of broader services • Intra-group knowledge sharing increases quality 	<ul style="list-style-type: none"> • Simpler to monitor quality and initiate new regulation due to fewer dental practices • Codified processes and/or standards in place 	<ul style="list-style-type: none"> • Consolidation reduces number of counterparties • Standardised back-office improves information on number of treatments and declarations • Ability to steer patients to high quality practices, enhancing insurers' reputations
Transparency	<ul style="list-style-type: none"> • Negotiating power shifts to regulators and payers based on professional reporting of treatment and quality 	<ul style="list-style-type: none"> • Transparency in pricing and procedures • Improved consistency of treatment 	<ul style="list-style-type: none"> • Lower number of dental practices eases regulation and oversight • Easier cost reviews 	<ul style="list-style-type: none"> • Standardised back-office of dental practices increases transparency of treatment administration
Efficiency	<ul style="list-style-type: none"> • Operational and potentially cross-border synergies like volume purchasing and access to more dentists • Optimal geographic coverage • Flexible operation with multiple disciplines under one roof • Optimal resource planning 	<ul style="list-style-type: none"> • One-stop shop • Standardisation and professionalisation leads to optimal experience 	<ul style="list-style-type: none"> • Easier to maintain acceptable price levels as dental practices are more cost efficient 	<ul style="list-style-type: none"> • More efficient operations for insurers, as lower number of counterparties reduces administrative burden
Monetary	<ul style="list-style-type: none"> • Lower capital expenditure requirements per dentist compared to solo practices • Revenue potential from operating multiple chairs per dentist • Revenue potential by integrating lab and technical innovations 	<ul style="list-style-type: none"> • Prices might be lower than current price levels due to cost efficiencies 	<ul style="list-style-type: none"> • Lower overall costs 	<ul style="list-style-type: none"> • Long-term reimbursements decrease when quality of treatment and general oral health increases

Source: KPMG analysis and market interviews, 2016.

Keep it local – and keep it personal

Centralisation may deliver efficiencies, but any consolidation strategy should also incorporate an in-country operation with local knowledge and contacts. Regulations and health insurance policies can differ greatly from country-to-country, making a 'one-size fits all' pricing model impractical.

Dentistry is essentially a local business attracting local patients, so it is advisable to maintain country-specific brands within the overall company portfolio. This not only reassures customers, but also helps minimise the reputational risk should other brands within the group suffer adverse publicity. For example, Hesira operates under the brands Dental Clinics Nederland (in the Netherlands) and Adent Cliniques Dentaires (in Switzerland).

Most people do not want a trip to the dentist to feel like a faceless 'corporate' experience.

When employing dentists from other countries, the chain's management should ensure that, where possible, they are fluent in the local language and well acquainted with local ways of working. It is also advisable to minimise the incidence of short-term staff appointments, to maintain the kind of continuity that patients value. One survey participant noted, "you need to find staff that are willing to work for

you for 10-20 years. Customers want to be treated by the same dentist but for a chain this is difficult to offer." This sentiment was voiced by another dentist we interviewed, who said that, "the main challenge for chains is employee churn. Going to a chain where you have a new dentist every time and someone who doesn't speak your language doesn't help."

Finally, in building a large business, dental chains have to be aware of the intimate nature of the patient-dentist relationship – something that many of our expert interviewees felt very strongly about. Most people do not want a trip to the dentist to feel like a faceless 'corporate' experience, so when acquiring other chains or individual practices, it is vital to select those with a focus on high quality care with a personal touch, and to integrate each practice gradually and carefully into the brand, with an emphasis upon longer-term growth rather than short-term profitability. With such a mindset, investors should be well placed to make the most of exciting market consolidation opportunities. The increased efficiency of chains can also benefit the wider healthcare ecosystem, by introducing greater consistency and quality of treatments, reducing the cost per patient and improving preventive oral care.

Six tips for building a successful chain of dental practices



Ensure a local 'feel' to each practice within an umbrella brand



Retain an in-country management team to handle regulatory issues like payment policies



Build a flexible workforce that can operate across more than one site when necessary – but strive to retain as much staff consistency as possible by practice to enable continuity of patient care



Invest in staff retention by offering training and opportunities for advancement



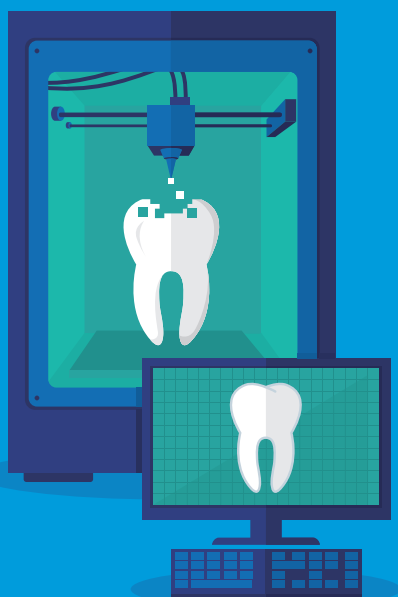
Vertically integrate by buying/building dental laboratories – and where suitable, consider the potential to offshore these



Consider investing in CAD/CAM and 3D printing technology to increase supply chain efficiency.

Our team of M&A professionals has an in-depth understanding of the European dental environment, having worked on numerous deals in Belgium, Germany, the Netherlands, the Nordics, Spain, Ireland and the UK. As such we have local teams with local knowledge of these markets.

We have carried out buy- and sell-side financial, tax and pensions due diligence, analysing demand patterns, regulatory dynamics, value chains, business processes, pricing and technology. Our team has helped with business strategy development — including market entry analysis – and provided financial management advisory services for dental groups, both locally and regionally. We have knowledge across the dental value chain, including dentists, group practices, laboratories, equipment manufacturers, governmental institutions, healthcare insurers and dental associations.



Notes

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About KPMG's Global Strategy Group

KPMG's Global Strategy Group works with private, public and not-for-profit organisations to develop and implement strategy from 'Innovation to Results' helping clients achieve their goals and objectives. KPMG Global Strategy professionals develop insights and ideas to address organisational challenges such as growth, operating strategy, cost, deals and transformation.

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