

Looking back, looking forwards

Abi Greenhough gives a review of the dental market in 2023, and offers predictions for 2024.

Finance



The acid test of the value of any dental practice is the response you get from buyers when it is presented the market. An initial valuation is often the start point of our

business relationship with a vendor, but in essence a valuation is an educated assessment. A valuation is not a guarantee of the market value.

To get to a realistic valuation one of the data streams we mine are the prices we achieve at the point of completion. In this article we want to share with those dentists interested in buying, selling and financing a dental practice what those numbers were for the second half of 2023. What the drivers are behind those values and what we believe the trends in the market are as we get into 2024.

In 2023 the market quickly adjusted to the increased cost of borrowing which started in the second half

of 2022. As we know, the upward trajectory continued until August 2023 when the interest rates stood at 5.25 per cent.

Between February 2009 and June 2022 entrepreneurs have been borrowing money at interest rates of less than one per cent plus bank margin. Now buyers have adjusted to the new normal of the Bank of England interest rates being 5.25 per cent. Anyone in business in the early 1980s operated with the interest rates at 15.13 per cent. All markets find a way to adjust to current circumstances and dentistry often leads the way. The market did readjust in 2023. There was initially less buyer ➔



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demand. That is not to be confused with 'no buyer demand'. Corporates either stopped buying or reduced their growth targets. Investor buyers paused in order to see where the market would land before getting back in. Lenders became more rigorous in considering lending applications.

In the second half of 2023 we saw the corporate dental groups return to the market, but with a new strategy. They have smaller growth targets than before but they are also much more interested in practices which have growth opportunities. The corporates are much keener to grow their EBITDA (earnings, before interest, taxes, depreciation and amortization) through organic growth and not just through acquisition. This is because with each increase in interest rates their cash flow becomes squeezed.

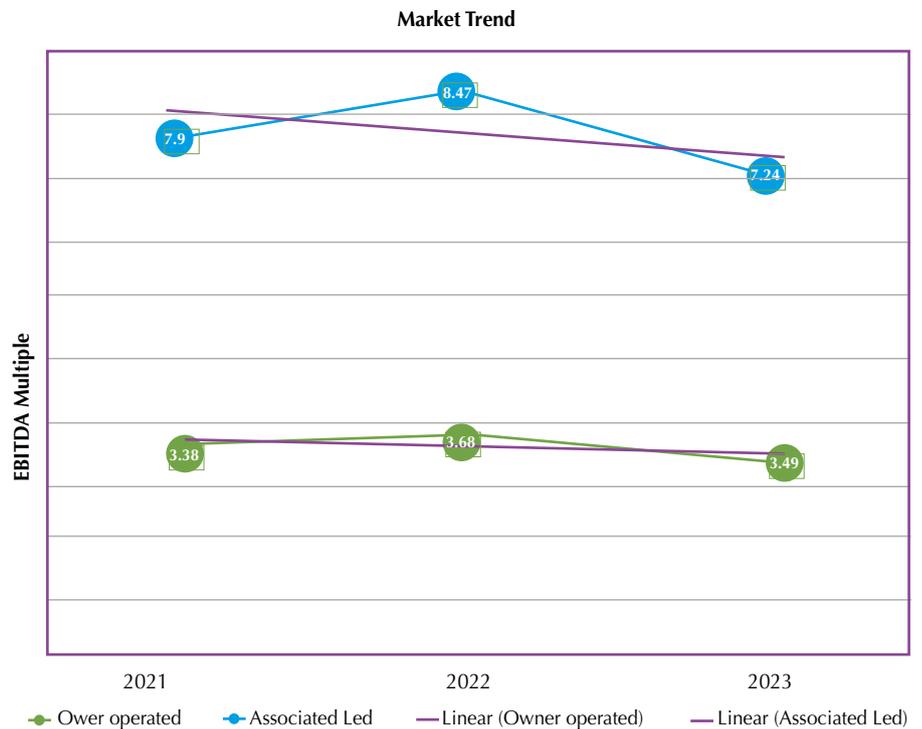
In 2023 we saw an increase in the volume of orthodontic practices coming to the market. Those owners who had secured a 10-year orthodontic contract in 2017 were starting to plan their exit before their contract started to decline in value. Those principals with shorter contracts are taking action because the NHS continues to kick the can down the road about tendering and renewing these contracts and Principals are not prepared to wait for them to make a decision. Principals are not motivated to stay on when only being offered one to three-year renewal agreements.

The key considerations for all buyers now are:

- Has the practice revenue been maintained since covid?
- The relative merits of the existing practice team and the opportunities to recruit staff in the area.
- What the UDA rate is and how the practice has performed against its NHS contract.
- Over reliance on one clinician or one off treatments such as short term orthodontics.
- How sustainable is the profit margin?

Increasingly the focus of buyers has become practices which:

- Have scope to grow their revenue.
- Have room for one or two more



surgeries which can generate around £200k each in additional revenue.

- Can grow their range of services. 'Buy – invest – grow' is the mantra of many buyers when considering their opportunities.

We should also consider current buyer behavior. Buyers are forensically analysing all aspects of a practice before commitment to the purchase. This is to satisfy themselves and their lenders that the practice has a sustainable bottom line and that there are organic growth opportunities.

Organic growth opportunities are seen as opportunities to offset higher interest rates and the squeeze on earnings that represents.

This chart shows the average multiple of EBITDA on completed practices over the last three years. Multiples of EBITDA at the end of 2023 for associate lead practices was 7.24 (range 5.7-10.44). Multiples of EBITDA at the end of 2023 for owner led practices was 3.49 (range 2.0-5.69).

The take aways are:

- 1) The value of owner operator practices sold to other dentists remains stable.
- 2) During the Summer 2022 there was a post covid peak in values achieved.

- 3) 15 per cent reduction in the multiple of EBITDA paid by corporate and mini groups in the last half of 2023.

- 4) The trend for corporate and mini-group purchases over the last three years shows a drop of nine per cent. Six per cent of the fall is an adjustment to the 'bull market' of 2022.

- 5) Private practices and NHS/mixed in the right location with growth potential are attracting the most interest and the highest prices.

- 6) Well run NHS practices are still attractive, but no longer attract a premium.

I am pleased to report that confidence is restored in the market as entrepreneurial dentists have adapted to the 'new normal' of higher interest rates. Throughout 2024 I am expecting buyers and their lenders to apply a forensic approach when reviewing each opportunity that they consider. Practices which have unfulfilled growth opportunities will attract a premium where they might not have in the past.

There is less competition between the corporates. We are already seeing this is creating more opportunities for new buyers and investors.