



Episode 103: Hot Sectors in Health Tech Today, With Bill Watts

Episode Summary

What is a white-hot market in healthcare tech? Governance, risk and compliance (GRC), says [Bill Watts](#), who leads the healthcare tech group at Brown Gibbons Lang & Company. He also lists supply chain for pharma and drug commercialization and employer tech.

In this conversation with McGuireWoods partner and host [Geoff Cockrell](#), Bill unpacks how today's health tech investment landscape has evolved post-pandemic, with investors pursuing different strategies as deal volume normalizes.

Tune in for his insights about mixed business models, deal activity so far this year and the commercial prospects for AI.

Transcript

Voice Over ([00:00](#)):

This is The Corner Series, a McGuireWoods series exploring business and legal issues prevalent in today's private equity industry. Tune in with McGuireWoods partner Geoff Cockrell as he and specialists share real world insight to help enhance your knowledge.

Geoff Cockrell ([00:22](#)):

Thank you for joining another episode of The Corner Series. I'm your host, Geoff Cockrell, a partner at McGuireWoods. Here at The Corner Series, we try to bring together dealmakers and thought leaders at the intersection of healthcare and private equity. Today I'm joined by Bill Watts, managing director at BGL. Bill spends most of his time on sell-side advisory work, largely in the software and tech enabled services arena of healthcare. Bill, if you could introduce yourself and BGL, and then we'll jump into a discussion on health tech investing.

Bill Watts ([00:54](#)):

Thanks, Geoff. And thanks for having me. Bill Watts, I lead BGL's health care tech group. Personally out of San Diego. Our healthcare group is based largely out of Chicago, with about 25, 30 bankers. And then BGL itself is a large middle market investment bank across four or five offices in about 120 to 130 investment bankers. I'd say my focus in general is around, to your point, software and tech enabled companies. These are businesses that are providing services as a software company, largely trading on a revenue multiple, or tech enabled business that as cash flows or EBITDA, but is doing something disruptive in the market and high growth. Those are the types of companies I represent on the healthcare tech side. So nice to meet you, and glad to be here.

Geoff Cockrell (01:46):

So Bill, health tech investing covers a lot of ground and you kind of gave some segmenting. But from an investor perspective, how would you think about formally segmenting the health tech market?

Bill Watts (01:59):

No, it's a good question. I can go into the large buckets that you typically see, and then we can dive a little deeper in some of the core markets we play in. But when you think about just the buckets itself, it follows the service a little bit. So if you think about providers or provider tech, that's a large part of the market. That's, generally speaking, solutions or technology that are helping providers do their job better, typically at the point of care, potentially with the EMR, or even taking a step further into potentialing and licensing.

(02:32):

Then you have the cost part of the spectrum, which is more on the employer and payer technology, which is those folks or those groups looking to lower the cost of care. Typically, those are the capitated entities that are on the hook for payments. And with that market, you see a combination of population health, where value-based care models are continuing to evolve, where they're trying to find the highest cost patients and intersect and move those higher cost patients into a care coordination. You see Rx spend or drug spend on the PBM side trying to manage that across payments, RCM, and really more on the specialty side where the majority of that cost is located.

(03:22):

Then on down further into payer and employer, you see more on the benefits side and on the workforce management side, and that's largely when you get into touching almost into insurance, but you're in the self-insured employer side either working through brokers or self-insured employer side. And I'd say the last one we think at a very high level is pharma technology. Those are clinical trial management, drug commercialization, patient recruitment. Anything around enabling pharma to be able to, one, research and develop branded medications, and then commercialize those medications and distributing them into patients. So I'd say those are the high level buckets that we think about.

Geoff Cockrell (04:07):

How much of the market is controlled by traditional cash flow businesses versus explosive software businesses? Those seem like very different markets to me. How big are they?

Bill Watts (04:22):

They are. And when you say control, the strategies that play in all these respective spaces, whether they be public or large privates, are largely cash flowing businesses, although they all have some sort of technology underpinning them and the technology that's attacking certain solutions. But they're generally thinking about, when they're thinking about acquisitions and integrations, they're generally thinking about more on the cash flow side. And then when you think about moving downstream to more point solutions that can tackle a problem a little bit faster than strategic, it sort of runs the gamut. It's really dependent on the space.

(05:01):

So a lot of times if you see a GRC company, for example, that's doing compliance, credentialing, licensing, they have the capability to contract longer term contracts a lot of times with health systems, for example, where they're getting 2, 3, 5 year contracts to provide a service. Those generally can develop into more subscription based models that are more revenue driven. I'd say those of size usually get acquired into those few larger players out there. And so, those don't seem to, same with payer services, don't seem to have a long runway before there's an acquisition.

(05:40):

And then, when you touch more on the care coordination side, care management side, population health, you start to get a little bit more into the service side, where there's more people involved, there's patients, you have to go out, and intervene, and care coordinate the higher risk, higher cost patient and to a care setting. Those generally will be more cash flow based. And that's really where you get into the tech enabled side. And then you have the balance between how much can you do with technology and then how much do you really need a person providing a service. So it sort of runs the gamut, I'd say.

(06:15):

On the provider side, you see more and more on the EMR side that is more software based, more tech-based, although those are a little bit smaller from a size perspective because the EMR is really dominated by a few players. And then on the GRC side, you see more fragmentation, in my opinion, with more players, less consolidation up to this point, although I think that'll continue to change. And then, on the PBM side, you have the big three. And so, those big three largely dominate the market. You have smaller mid-market PBMs and then you have solutions around that, that are trying to disrupt the market, but that is a tougher market to penetrate.

Geoff Cockrell (06:57):

And what about the buyer landscape? If you set aside strategics on the financial investor side of the table, to what extent is it dominated by healthcare investors that also do tech or tech investors that are doing healthcare? I see folks often describing themselves as one or the other.

Bill Watts (07:16):

Yeah. No, it's interesting, and it's gotten really complicated. I'd say on the back of the pandemic and COVID, where there was a ton of just volume and opportunities out in the market on the healthcare tech side, the investor landscape has continued to ask themselves, "Okay, when are we going to get back to those levels?" And over the last 18, 24 months, I think investors are appreciating that this is probably the new normal, normalizing the volume we have today, where there's a handful of A assets out there that get all the attention, there's several Bs that get more attention, then there's the Cs and below that have floundered out in the market a little bit and tried to find the right home.

(07:59):

I think with consistent volume, though, to answer your question, there has been more and more investors focused on healthcare technology. And there's different groups. You have the traditional middle to lower middle market private equity that have been more on healthcare services and are looking at their business or their portfolio and saying, "We want to get more into healthcare technology." I generally see those groups more on the tech enabled side, more finding higher growth, but still wanting to pay on mid to high teens EBITDA multiple. So you see those entrants coming into the market more and more, and largely pivoting their investment thesis and trying to diversify their portfolio.

(08:45):

You have the healthcare tech focused private equity middle market investors that have always been here and are very targeted around what they're looking for, very thesis driven, like to bring an operating partner with them. Those have large... What's kind of been interesting is a lot of those funds, there's folks that have done really well, they've split out and done their own fund, and so that has grown just in magnitude.

(09:09):

And then you have more of your vertical SaaS private equity investors. They largely just want SaaS. And so, it's hard to find SaaS in healthcare. They generally focus more on the fringes, where you can actually... You don't have a Medicare Medicaid risk. You're able to contract with a self-insured employer, a health system, a payer, and get long-term contracts and have higher gross margins because you're providing a software. Those are more focused on SaaS.

(09:39):

But I think what they're appreciating is that, and as the volume stayed consistent, but there's more and more investors trying to get into the market, those vertical SaaS players need to be more verticalized in healthcare. And so, they've been sort of tagging people more and more like, "Hey, you're going to be the healthcare investor. You need to go out, build relationships, demonstrate why we are the right investor for that lower middle to middle market founder that wants to take their company from A to Z." And so they've become more strategic. So the landscape has gotten more competitive over the last 18 months, but the volume has stayed consistent. So it's been a very competitive dynamic that's been going on in the market.

Geoff Cockrell (10:25):

And looking at the segments, what would a heat map look like as far as levels of interest in activity? What are the hotter quadrants?

Bill Watts (10:34):

Yeah. The white-hot markets are GRC for one, governance, risk, and compliance. Everyone's focused on that. It's hard to find opportunities of scale in that market. And largely, if something gets of scale, it's gotten acquired by a couple of the bigger players. But that is a market that there's just a lot of focus around and you can blur the line on when you start GRC. But I'd say a lot of that has to do with how those companies contract. They're largely contracting long-term contracts, higher gross retention, because shifting a vendor for a health system on the GRC side can be complicated.

(11:19):

And so, that's a white-hot market. Supply chain continues to be a very good market. I've seen a lot of interest on the supply chain for pharma and drug commercialization. I think there's been a lot of movement there. There's generally always been a lot of supply chain interest on the GPO side, in and around how health systems are getting their supplies and things like that.

(11:46):

And I'd say employer tech over the last six, nine months has become another really exciting space, to where every call I have, someone's like, "Hey, you looking at employer tech?" And it's a little bit blending into the insurance side, if you will, but not into your stop loss. More onto the employee benefits side, where there's a management of the employee's benefits, handling claims, which is always generally a hard thing to do and ripe for automation. So that's really an attractive market.

(12:22):

I think the markets that continue to be down and out are your more virtual care markets, where you're trying to tackle primary care and things like that that have been hard to scale from a profitability standpoint. And then D2C, direct to consumer continues to be not an attractive market for the most part for a lot of healthcare investors. I see more of that interest as shifted more into the consumer side on the investor market.

Geoff Cockrell (12:51):

We're a little ways into the new administration, and a lot of investors are still trying to figure out what the impact of administration policies are going to be on investing. What are some of the key impacts that you're foreseeing on health tech investing, whether it's tariffs or other elements?

Bill Watts (13:10):

Yeah. I think there's the first order effects of just the supply chain issues, interest rate environment, that I think the losers or what's slowed down that groups that are looking to use debt for their acquisitions or do more financing because the interest rate environment just is very... I think that the hypothesis was rates were going to go down on the back half of 2025, and now there's just confusion

around whether that's going to happen or not. So where the market is remaining strong are those groups that are more focused on cutting your equity checks.

(13:50):

That is the sub 250, sub 300 million EV market, enterprise value market, where it's more about deploying equity checks, finding more founder based businesses, and growing those businesses. I think it's being a little more challenged in these acquisitions where you're relying more on debt, you're leveraging the current EBITDA on the business, and then the rate environment has not gone down as you've expected. So that's the first order where I think a lot of the healthcare tech has been a little bit, not 100% immune, but able to push through because a lot of the acquisitions that I see in this market, it's more equity checks. Folks aren't necessarily taking a lot of leverage for deals.

(14:37):

I'd say the second order of effect that I think will play into it is one that's plagued the market in general over the last 12, 18 months, which is, on the back of COVID, a lot of companies have wanted to right size their businesses. Cash burning profiles were no longer attractive. You wanted to be breakeven, or a path to profitability, or even having a little bit of EBITDA was extremely attractive for a software company, for example. So there was less spend on growth, less spend on sales team, with the desire to move more into a state of profitability. That has, for some companies, slowed growth. Moved them from the rule of 40 to more of the rule, slower grower, 15, 20% year-over-year growth.

(15:28):

And so those companies have had a little bit more of a challenge in the market, just because if you are a disruptor in the market, the investor would expect you to be a higher grower. And so, the slower growth has confused the market between the investor and the company, but companies have largely wanted to become more profitable. I think what's going to happen from a second order of effect with the new administration is the customers of these tech companies, the self-insured employers, the brokers with self-insured employers, the health systems.

(16:02):

All these corporates are going to be more risk averse in terms of taking on new contracts with new tech companies until they see the market stabilize, until they know what's going to happen with supply chain, and yada yada. And so, I think there's going to be a bit of a challenge on the executioner side for a lot of these healthcare tech companies over the next nine, 12 months. Not necessarily getting hit on the first order side with interest rates, and debts, and things like that. But I think more on the second order.

(16:36):

Where I do think it's a little bit nebulous right now is on the pharma side and on the PBM side around what the new administration is going to do around transparency there, which I think will help be a tailwind for a lot of the companies trying to penetrate that market, and doing something different, and

lowering the cost of care, and bring price transparency to patients. But I think that's still a little bit unknown in that market.

Geoff Cockrell (17:02):

What about in the health tech investing arena? What do you think are some of the major disruptors? Obviously the place to start is with AI. But what are some of the big disruptors that are either presenting or about to?

Bill Watts (17:16):

Yeah, it's interesting. AI, in my opinion, and others may disagree, AI still feels more like it's a couple years away from showing true commercialization that an investor can actually underwrite. Right now, I think investors like to see an opportunity for AI to be administered and to continue to grow the scale of a company based on what it's doing. But I'd say there's very few companies that are using AI as the tip of the spear, this is what we're doing. And then investors directly underwriting that AI. Investors continue to underwrite.

(18:01):

In my opinion, the core fundamentals that have driven valuation over the last few years is growth. I think paramount. I think we have seen a shift in the last 12 months where you can invest for growth and you can be burning to some extent. It can't be dramatic burn, but you can be burning cashflow with the path to profitability so long as you are hitting your proverbial rule of 40, or so long as you're showing demonstratable growth over the last year or two and a clear path to strong growth. I think that in itself is becoming more rare, just based on what I talked about before, is that there has been less growth in the market with the move more towards profitability.

(18:51):

I think the other thing that's really continued to drive the market is re-recurring contracts with these tech companies and how investors underwrite it. Although I will say there has been a move toward more mixed business models. And what I mean by that is, if you think about your vertical SaaS investors or you think about your more healthcare textbook investors, over the last four or five years, they've wanted pure SaaS. I need to go through the contracts, I need to make sure this is truly contractually committed over the term and so on.

(19:27):

And payments, for example, which has been a really nice business, payments either collecting a small transaction fee on a payment, creating payment transparency between the payer, the patient, and the provider, those have been more volume-based. And so you haven't seen that contractually committed 2, 3, 5 years. It's been more volume-based.

(19:50):

But nonetheless, those companies have seen a ton of growth. And then they have also seen material EBITDA around that growth. And so, the more pure SaaS investors historically have started to move more into what we're willing to do, more mixed business models, more volume-based models, as long as we see a sticky customer base, we see the natural business dynamics you'd like to see in the software business around gross retention, gross margins, things like that.

(20:21):

But I think that on the tech side too, I think to answer your point directly around what's the tech aspects that folks really have been really driving value, it's around really I'd say more around the automation side than I'd say the AI side. When I think of AI, I think of completely establishing the ability to remove the human element, and you're able to, call centers, for example, where you almost always have to have a person, can you completely navigate the patient through a call center completely through AI, or something like that.

(20:55):

Or I'd say those I don't see as much on, but I do see a ton around automation, let's say around claims, around working with government agencies, states, the federal government, around licensing, where for example, if you want to do licensing with some states, sometimes they have a portal. You got to click through, you got to do, got to do a form inbox in order to submit that license. There's all these things that always require human element that have an inherent cost to it. And I'd see more and more automation in certain markets that just allow the human element to be removed to the extent possible. I think that's really what's driving a lot of value.

Geoff Cockrell (21:40):

So, last question. As we look start to see the second half of 2025 materializing, what's your prognosis for aggregate deal activity for the second half?

Bill Watts (21:52):

Yeah. It's interesting. Last year at JPMorgan, the feeling was that 2024 was going to be the bounce back from 2023, and you're going to see this dramatic lift in volume on the healthcare tech side. And it was good volume, but you didn't see the hockey stick that was being advertised or believed to come true. I think the same thing is happening this year in terms of JPMorgan, where the beginning of the year, you saw a lot of companies saying, "This is the year we're going to come to market. We're targeting 6/30. We're targeting September. It's coming, and there's going to be this avalanche."

(22:41):

There's been generally good volume and flow the first couple months, but there hasn't been this dramatic, again, hockey stick. And I think it's going to continue to be somewhat consistent and the moderate volume levels versus this dramatic pouring out of actionable opportunities. And I think that's a function of, one, the uncertainty in the market around administration and around these core markets. What's going to happen? I think the interest rate environment will continue to have this effect on certain markets.

(23:21):

But then, I just also think there is this return to normal, that some folks are appreciating that this is the volume that will continue to exist, and we'll probably never get back to pandemic levels. And I think that that volume will continue to the end of this year, I guess, is how I think it's going to play out. So not too high, but not too low. We're not going to end up with not a lot of M&A. I think it's just going to be a moderate level.

Geoff Cockrell (23:54):

It won't be 2021 again, which is just fine. Well, Bill, we could talk for quite a bit, but let's call it there. It's a super interesting area that you spend your time in. Appreciate your insights. Thanks for joining us. It has been a ton of fun.

Bill Watts (24:15):

Thank you, Geoff. Appreciate you having me.

Voice Over (24:15):

Thank you for joining us on this installment of The Corner Series. To learn more about today's discussion, please email host Geoff Cockrell at gcockrell@mcguirewoods.com. We look forward to hearing from you. This series was recorded and is being made available by McGuireWoods for informational purposes only. By accessing this series, you acknowledge that McGuireWoods makes no warranty, guarantee, or representation as to the accuracy or sufficiency of the information featured in this installment.

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