M&A Trends in Healthcare

Mark Blake
EVP, Strategy and Corporate Development
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Agenda

Very brief introduction to Cardinal Health

Perspective of the presentation

M&A in the context of strategy

Dynamic responses across the industry

Why M&A is rewarded in the current environment

Strategy & financials

Questions
A very brief introduction to Cardinal Health

Pharmaceutical Segment
- Revenue: $91B
- Pharmaceutical Distribution
- Specialty Solutions
- Nuclear Pharmacy Services

Medical Segment
- Revenue: $10B
- Medical Products and Services
- Infection Prevention Portfolio
- Global Manufacturing & Sourcing

The business behind healthcare

Cardinal Health helps healthcare providers focus on patient care while reducing costs, enhancing efficiency and improving quality

Our Customer Breadth
- Retail chain pharmacies: 18,000
- Independent pharmacies: 7,000
- Physician offices: 7,700
- Ambulatory Care Sites: 2,400
- Independent labs: 3,800
- Hospitals: 5,500
Three of our latest transactions

<table>
<thead>
<tr>
<th>Company</th>
<th>Description</th>
<th>Transaction date</th>
</tr>
</thead>
<tbody>
<tr>
<td>CVS Caremark</td>
<td>Generic drug purchasing JV</td>
<td>December 10th, 2013</td>
</tr>
<tr>
<td>Intralign</td>
<td>Investment in a provider of orthopedic surgical services</td>
<td>October 28th, 2013</td>
</tr>
<tr>
<td>AssuraMed</td>
<td>$2.1B acquisition of a provider of home health medical supplies</td>
<td>February 14th, 2013</td>
</tr>
</tbody>
</table>

42 transactions over the past 4 ½ years
- Ranging from <$1M to over $2B
- Includes minority investments, partnerships and acquisitions
- Located in the U.S., Canada and China

M&A in the context of strategy
- M&A is a means to achieving a strategic goal
- An investment, acquisition or partnership should reflect a carefully constructed strategy
- Typically acquisitions have some of the following characteristics:
  - Strategic value that promises future financial returns
  - Near-in financial returns with a low risk profile
  - Accretive to earnings, growth rates and/or margin profile
  - A business that improves the portfolio in terms of risk and time horizon relative to other organic and inorganic initiatives
  - Reflects a view on the maturity curve of the industry
  - Adds a capability that is needed to meet a strategic objective
- End result of organic and inorganic investments is to promote short-term strength and long-term evolution of the company
What are the key success factors for a transaction?

- Clear strategic rationale for the deal:
  - Why this market?
  - Why this target?
  - Why us?
  - Why now?

- Financial metrics that align with the underlying strategic purpose

- Cultural fit

12 trends shaping the healthcare environment

1. Growing population of sick and aging Americans
2. Accelerated shift from small molecules to biologics
3. Care moving from acute care hospitals to more efficient models
4. Upstream and downstream consolidation and business model evolution
5. Information transparency
6. Regulatory changes
7. Considerably faster healthcare growth ex-U.S.
8. Waning trust in the healthcare system
9. Cost focus expanding from price to utilization
10. Consumers increasingly knowledgeable and involved in their healthcare
11. Increasing focus on coordination of care
12. Technology advancements and adoption
Patients might have the same diseases, but there will be a new class of consumers

Consumers are more informed and more accountable

Over 60% of consumers now look online for health information

% of Covered Workers enrolled in High Deductible Health Plans 2006-2012

Source: Kaiser, HRET survey of employer-sponsored health benefits

Forces of change

Price
Preparation to operate on “Medicare margins”

Utilization
From fee for service to fee for value

Demand
A sicker, older, smarter population
The net impact

- Cost pressures are mounting
- New levels of efficiency and quality are one way to drive sustainability
- For now, providers and the market at large must live in a fee-for-service world while also preparing for the realignment of incentives

Acquisitions are a telling indicator

- In the past 30 months
- Across 40 healthcare companies spanning the industry
- We have seen...

- 297 acquisitions
- $130B of disclosed transaction value
- $135B of disclosed target revenue
Prevailing themes

Vertical Integration
- Follow the Patient
- Technology Integration
- Consolidation & Vertical Integration
- Geographic Expansion

NEW MODELS
- Innovative + Value Product Portfolios
- Payor-Provider Risk Sharing

SCALE

Channel consolidation

Rationale
- Bolsters channel strength amidst upstream and downstream consolidation
- Significant synergies on purchasing and fixed assets
- Consolidation wave largely complete and/or limited remaining targets of scale

Strategic Moves
- McKesson
- MedAssets
- Express Scripts
- medco
- Catalyst
- Tenet
- Vanguard Health Systems
Payor-provider risk sharing

**Rationale**
- Direct integration of payor-provider to align incentives on cost-effective care
- Advanced preparation for delivery model reforms
- Growing demand of supporting services that enable risk sharing without ownership (e.g., analytics, clinical integration)

**Strategic Moves**

Innovative + value product portfolios

**Rationale**
- Waning influence of physician preference
- Defensive move as channel players improve efficiency of low-cost switching
- Low cost product / operating model has option value longer term
- Bundling opportunity across a portfolio
- Innovation always has a place

**Strategic Moves**
Geographic expansion

Rationale
- Global scale creates product and sourcing leverage
- Manufacturers already global in scope
- Higher growth in emerging markets
- Volume of healthcare activity to offset price pressures worldwide
- Hedging of macro economic risk

Strategic Moves

M&A announcements significantly impact stock prices

<table>
<thead>
<tr>
<th>Company</th>
<th>Open</th>
<th>Close</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>CardinalHealth</td>
<td>$64.06</td>
<td>$66.22</td>
<td>+3.37%</td>
</tr>
<tr>
<td>Walgreens</td>
<td>$42.43</td>
<td>$44.74</td>
<td>+5.44%</td>
</tr>
<tr>
<td>McKesson</td>
<td>$88.68</td>
<td>$92.30</td>
<td>+4.08%</td>
</tr>
<tr>
<td>CVS Caremark</td>
<td>$66.60</td>
<td>$67.99</td>
<td>+2.09%</td>
</tr>
<tr>
<td>AmerisourceBergen</td>
<td>$48.30</td>
<td>$50.06</td>
<td>+3.64%</td>
</tr>
<tr>
<td>PSS/WorldMedical</td>
<td>$21.60</td>
<td>$28.57</td>
<td>+32.27%</td>
</tr>
<tr>
<td>Harris Teeter</td>
<td>$36.19</td>
<td>$37.15</td>
<td>+2.65%</td>
</tr>
<tr>
<td>CVS/LonghornMed</td>
<td>$48.52</td>
<td>$49.26</td>
<td>+1.53%</td>
</tr>
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Key metrics

- EBITDA multiple
- Synergies
- Net present value
- GAAP Earnings
- Non-GAAP Earnings
- Return on Invested Capital
- Return on Tangible Capital
- Internal Rate of Return
- Payback Period

Fictitious example

Selected statistics

<table>
<thead>
<tr>
<th>($ in millions)</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>$300</td>
<td>$375</td>
<td>$450</td>
<td>$500</td>
</tr>
<tr>
<td>Segment Profit (EBITA), including synergies</td>
<td>$15</td>
<td>$35</td>
<td>$45</td>
<td>$55</td>
</tr>
<tr>
<td>Transaction Amortization</td>
<td>$25</td>
<td>$30</td>
<td>$20</td>
<td>$15</td>
</tr>
<tr>
<td>EBIT (GAAP)</td>
<td>($10)</td>
<td>$5</td>
<td>$25</td>
<td>$40</td>
</tr>
<tr>
<td>Non-GAAP EPS</td>
<td>$0.02</td>
<td>$0.06</td>
<td>$0.08</td>
<td>$0.10</td>
</tr>
<tr>
<td>ROIC (%) excluding amortization (Non-GAAP)</td>
<td>6%</td>
<td>8%</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td>ROIC (%) including amortization (GAAP)</td>
<td>(4%)</td>
<td>2%</td>
<td>7%</td>
<td>13%</td>
</tr>
</tbody>
</table>

- Net Present Value: $240M
- IRR: 18.3%
- NOPATA Purchase Price Payback: 6.8 years

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Key metrics

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Why is M&A exciting in healthcare today?

- We are in an environment of unprecedented change
- Price pressure is not new but continues to accelerate: customers no longer pay more for incremental innovation, they need more value
- Focus on utilization IS new: more and more pressure to curtail healthcare consumption
- Manufacturers, distributors, providers and payors need scale to compete
- There is just as much innovation as ever but it is often found in new areas
Q&A