



By Simon Palmer

The calm after the COVID storm for practice values

As Australia combats COVID-19, there is a lot of uncertainty about what the future holds. The current situation is essentially unprecedented in human history.

While there are some “chicken littles” out there, running around saying that the “sky is falling” and hoarding enough toilet paper to satisfy a small country, most people believe that the restrictions in place for COVID-19 will subside within a few months. When it does, there will be many dentists who will be worried about the impact the economic shutdown will have had on the value of their practice, particularly if they are at a stage in life where selling is typically the next step.

While no one has a crystal ball here, there are plenty of reasons not to be distressed.

The underlying assets are robust

The first point to remember is that the assets of any business are made up of tangible and intangible assets.

1. Tangible assets

Tangible assets are those that you can see and touch. In a dental practice, this means the equipment, fit-out, fixtures, fittings, etc. These have been untouched by the current crisis.

2. Intangible assets

Intangible assets are those that you cannot see or touch, but still provide significant value to a practice. The most valuable of which is patient loyalty.

Normal trading of a dental practice may be interrupted over the coming weeks

and months and, as such, it is natural that practice revenue and profit will fall.

Ordinarily, if someone assessing a practice saw a business interruption (due to a broken hand, sickness, etc.) and a drop in the fortunes of the practice that lasted several months, they would start to assume that the patient loyalty has been compromised or lost. This will obviously not be the case with the COVID-19-related downturn. Patients are not being lost to a competitor down the road with better marketing, a price differential or better service levels.

Every practice in your area has been equally affected by this crisis. Patients haven't gone elsewhere. They have been temporarily held away due to quarantining and social distancing. Once these concerns are relaxed, there is no reason to believe that the patients will go elsewhere. As such, the underlying goodwill in a good practice should be seen as robust and will be there long after COVID-19 has passed.

Supply and demand

The value of almost everything we buy and sell is a function of the supply and demand for that asset. If a good or service is hard to come by and demand is strong, the value of that good or service goes up. The reverse of this is also true. If a good or service is plentiful and demand is weak, the price goes down. With that established, let's look at the ways that the COVID-19 economic shutdown will influence supply and demand for dental practices.

Supply of practices for sale

Common thinking is to say that a crisis like this will result in an oversupply of distressed practices on the market and this will drive the price of practices down. This (in my opinion) will not be the case.

1. The current crisis will mean that some great practices should become available

In the wake of this crisis, there will definitely be some great new opportunities available that have been shaken loose by the recent turmoil.

This will be either by:

- Practice owners who have had the stress of ownership magnified over this period and may want to move on for lifestyle reasons; and
- Practice owners who may have been too highly leveraged, with too little in their reserves, may be compelled to sell to release the capital they had locked up in their practices.

It's important buyers realise that these practices have not become available due to poor performance of the underlying asset. They have become available due to the circumstances of the vendors themselves.

2. The current crisis will mean some dentists put off selling

After the GFC, there were plenty of dentists close to retirement who had their retirement savings greatly reduced due to exposure to stock market downturn and had to put off their retirement plans. This crisis will be no different. Many, many people who had been diligently saving and had worked out a budget for how they could retire in the near future will need to delay their plans, at least temporarily.

Supply conclusion

It's too early to say anything definitive, but it is my belief that the impact on the supply of practices for sale will be fairly net neutral. That is to say, that the supply increases due to point 1 will be balanced out by the supply decreases due to point 2.

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Demand for dental practices

1. Some buyers and banks will be initially cautious

Once COVID-19 business interruption is behind us, some buyers will hold back, cautious, waiting to see how the world economy and consumer behaviour recovers. Buyers will be dipping into their savings over the period of business interruption and, as a result, will have less to use as a deposit or for security with the banks. This caution will no doubt mean that there will be a temporary reduction in demand.

2. COVID-19 will (in time) increase demand for practices

At times like this, the need for job security is brought home to every employee and contractor in the world. Working as a dentist for someone else on a commission means that your pay is dependent upon your practice rostering shifts to you and allocating patients your way.

When times are tough and patients are scarce, an owner operator may look to allocate their shifts and patients away from non-owner dentists. The owner may need to spread patients thinner between dentists working at the practice. They may decide to do the work themselves.

Owning your own business can be the best possible source of income security. When the dust settles on this crisis, I believe that more dentists than ever before will want to own their own business.

3. Low interest rates

Australia is experiencing historically low interest rates. In my opinion, these rates are likely to remain low for an extended period. This means that the government is setting things up for the market rebound, as it will be easier for buyers to:

- Repay their existing loans; and
- Afford more expensive practices.

4. Instant asset write-off

The recently introduced opportunity for instant asset write-off being increased to \$150,000 should be a huge incentive for buyers to:

- Proceed with purchasing practices that need a significant upgrade. There are some older practices that may have otherwise been passed over by buyers due to the reinvestment needed post purchase. This economic stimulus package will make these practices significantly more affordable; and
- Create their ideal practice out of the underlying foundation that they buy. New computers, an OPG or CBCT, etc., are now far more affordable to add to the practice they buy.

While this scheme is currently limited to assets that are purchased before 30 June 2020, there is reason to believe that this or something similar will be extended into the next financial year.

5. More government stimulus

There is a good chance that government will introduce more mechanisms like 3 and 4 to help spur on buying behaviour during and after the economic shutdown.

Demand conclusion

Post COVID-19, demand for dental practices will no doubt be affected by the 5 points above, which both increase and reduce demand for dental practices. Many buyers will be naturally cautious and want to wait to view how the economy recovers before moving ahead with a purchase. However, it is important for these buyers to note that Points 3 and 4 have been specifically introduced by the government

to stimulate spending in the market during this time of uncertainty and caution. When confidence returns to the market, there will be no need for the government to keep these stimulus measures in place.

It will be interesting to see how these competing forces play out in the post COVID-19 world.

This reduction in demand will need to be weighed against the above points, which provide significant new incentives to purchase that have not been there previously.

Overall conclusion

At a time like this, there is plenty of negativity out there to latch on to. Yes, revenue and profit will be down over these months, but that doesn't necessarily mean that your practice has less value. Owning a dental practice was never an investment to be looked at with a short-term lens. You need to look at its return over a longer period of time in order to see its true value. A level-headed and unemotional assessment of the situation should tell anyone assessing a practice to have confidence that patients haven't been poached and will return in due course.

There are many doomsday predictions for the value of dental practices, saying that there will be an oversupply of sellers and little demand. From my position at the front line of hundreds of practice sales, I see little reason to be worried. What I hope is evident from this article, is that there will be reverberations coming out of this crisis that push supply and demand for dental practices in both directions, and these forces should, to a significant extent, balance each other out. The COVID-19 business interruption has not undermined any of the value inherent in dental practices and they will remain a secure and valuable business for a dentist or investor to own for a long time to come.

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