CAUTION AHEAD

In the past 2.5 years, society has endured significant upheaval due to the COVID-19 pandemic. In the past 6 months, it has endured even more—a global stock market crash, significant inflation, an energy crisis, and political turmoil in regions formally considered bastions of democracy—as a result of the unexpected military aggression in Europe. We are in the midst of an interesting and worrisome time in history.

Until recently, private equity (PE) firms had a field day acquiring private ophthalmology practices, sharpening their balance sheets, and selling—or flipping—them a few years later to another PE firm at a higher multiple. Today, PE is on the ropes.[1] The PE space was last under such pressure in 2007, when the PE firm Blackstone lost 80% of its value. PE made an incredible recovery, but today's shifting investment patterns and higher interest rates mean it is unlikely to enjoy such a miraculous recovery again.

Global markets are reeling under the pressure of rising interest rates and the shrinking balance sheets of central banks. In 2022, equities suffered the worst sell-off in a generation. Debt markets, particularly the risky high-yield spaces where PE firms gather funds for deals, are also messy. PE deals have been one of the most significant investment trends in the past 2 decades, and PE assets have more than tripled over the past 10 years to reach €4.6 trillion.

During the recent history of low interest rates, almost all pension funds, endowments, sovereign-wealth investors, and life insurers invested heavily in private assets to try to bolster their returns. It is now common for a pension fund to have 10% of its holdings in this asset class.

According to *The Economist*, a double-fisted crunch may be coming.[1] First, deals that were done at high valuations are now less attractive. Inflation and higher costs have made flipping these assets much more challenging now than just 12 months ago. The second crunch relates to future investments. Buyouts, which involve using debt to buy private firms, can generate returns through rising valuations, high leverage, or improving operational performance. Two of these three levers are currently impaired. As interest rates rise, reversing a long-term downward trend, it seems unlikely that asset prices will improve anytime soon. Meanwhile, higher borrowing costs may be here to stay. Leverage is the lifeblood of buyouts, and the variables in the equation have fundamentally shifted in the past few months.

Who will suffer? According to *The Economist*, the initial losses will be incurred by the investment bankers who underwrote buyout debt at overvalued prices.[1] It is estimated that the biggest US investment banks have up to US$90 billion of corporate loans held for short-term purposes. These investors also face a bigger headache: They bet on high returns from PE to fulfill their promises to retirees and other beneficiaries.

I am also concerned about patients seeking ophthalmic services from private clinics. PE makes its money by bundling clinics together, cutting costs, increasing operational efficiency and buying power, and then selling the package to the highest bidder. If no buyers are willing to pay inflated prices, what happens to clinics where corners might have been cut in order to rapidly increase their value? Will patients suffer the consequences?

It should not be assumed that the public sector will pick up the slack; recent trends in Europe have shown exactly the opposite. During the COVID-19 pandemic, the private sector has picked up the slack from—and has been significantly more productive than—the public sector. It may be prudent for ophthalmologists who own, run, or work in a privately owned eye clinic to focus on patients and their needs and refrain from PE acquisitions for the time being. ■

1. Why leveraged buy-outs are in trouble. *The Economist*. July 7, 2022. Accessed August 18, 2022. https://www.economist.com/leaders/2022/07/07/why-leveraged-buy-outs-are-in-trouble

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