2023 Second Quarter Financial Results
Conference Call Transcript
August 7, 2023

Speakers:
- Carolyne Sohn, The Equity Group
- Brandon Sim, Co-Chief Executive Officer, ApolloMed
- Chan Basho, Chief Strategy Officer and Chief Financial Officer, ApolloMed

Operator: Hello and welcome to the Apollo Medical Holdings' second quarter 2023 financial results conference call and webcast. {operator instructions} It's now my pleasure to turn the conference over to Carolyne Sohn, Vice President of Investor Relations. Carolyne, please go ahead.

Carolyne Sohn: Thank you, operator, and hello, everyone. Thank you for joining us.

The press release announcing Apollo Medical Holdings, Inc.'s results for the second quarter ended June 30, 2023, is available at the Investors section of the Company's website at www.apollomed.net. To provide some additional background on its results, the Company has made a supplemental deck available on its website. A replay of this broadcast will also be made available at ApolloMed's website after the conclusion of this call.

Before we get started, I would like to remind everyone that this conference call and any accompanying information discussed herein contains certain forward-looking statements within the meaning of the safe harbor provision of the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by terms such as "anticipate", "believe", "expect", "future", "plan", "outlook", and "will" and include, among other things, statements regarding the Company's guidance for the year ending December 31, 2023, continued growth, ability to decrease cost of care while improving quality and outcomes, ability to deliver sustainable revenue and EBITDA growth as well as long-term value, ability to respond to the changing environment, ability to offset anticipated losses in the Care Enablement segment, ability to successfully implement operational streamlining, and successful implementation of strategic growth plans, acquisition strategy, and merger integration efforts.

Although the Company believes that the expectations reflected in its forward-looking statements are reasonable as of today, those statements are subject to risks and uncertainties that could cause the actual results to differ dramatically from those projected. There can be no assurance that those expectations will prove to be correct. Information about the risks associated with investing in ApolloMed is included in its filings with the Securities and Exchange Commission, which we encourage you to review before making an investment decision.

Carolyne Sohn: The Company does not assume any obligation to update any forward-looking statements as a result of new information, future events, changes in market conditions, or otherwise, except as required by law. Regarding the disclaimer language, I would also like to refer you to slide 2 of the conference call presentation for further information.

For those of you following along with the accompanying supplement, there is an overview of the Company on slide 3.

On today's call, the Company's Co-Chief Executive Officer Brandon Sim will discuss second quarter 2023 highlights and the latest operational developments. Chief Financial Officer Chan Basho will follow with a review of ApolloMed's results for the second quarter and six months ended June 30, 2023. Brandon will conclude the remarks with an update on the Company's outlook and long-term growth strategy before opening the floor for questions.

With that, I'll turn the call over to ApolloMed's Co-Chief Executive Officer Brandon Sim. Please go ahead, Brandon.

Brandon Sim: Thank you, Carolyne.

We were pleased to deliver another strong quarter, achieving 29% growth on the top line and 44% growth in adjusted EBITDA compared to the same quarter in 2022. Revenue growth was primarily driven by strong organic membership growth and a more favorable payer mix in our Care Partners business. We continued to execute on our three key operational goals: one, growing our membership in core and new geographies; two, empowering our Care Delivery and Care Partners providers to successfully move along the glide path towards value-based care, and three, enabling our providers to deliver excellent patient outcomes in order to manage that risk effectively.

On the first goal, growing our membership in core and new geographies, we continue to see strong growth as a result of the strength and quality of our Care Partners business as well as the technology, operational, and care management support we bring to bear in our Care Enablement business.

Our core business in California continues to demonstrate robust growth, both organically in our partnered groups as well as in new partnerships signed. We recently formed a long-term partnership with a primary care group in California with a network of over 50 providers, joining our newly signed class of partners in 2023. We expect to onboard this group onto our Care Enablement platform by September 1st of this year.

Brandon Sim: We also want to highlight what we believe is our ability to replicate our success in Southern California in other markets. As previously communicated, our playbook for empowering providers in a new market includes: first, entering a market in partnership with a high-quality anchor group for our risk-bearing Care Partners business; second, investing in local operational and care management teams to ensure successful onboarding onto our Care Enablement platform for these providers, and finally, partnering with additional groups in the market who would benefit from joining our platform. This flywheel accelerates as we reach critical mass in each market, and we believe that the enablement platform we've built and proven to generate great patient outcomes and profitability in Southern California will allow us to demonstrate this progression rapidly in each new market we enter.

In Texas, for example, we entered with the acquisition of Valley Oaks Medical Group last October. As we build out our local market leadership in Texas, we're pleased to share that Jaime Melkonoff, a healthcare executive with over 20 years of experience in the industry, has joined us as President of ApolloCare Enablement of Texas and Senior Vice President of Business Development. Jaime is expected to play a key role in expanding our Care Partners network across the country and further building out our Care Enablement platform's capabilities, empowering providers to advance along the value-based care glide path responsibly in Texas. We are thrilled to welcome Jaime to our leadership team and look forward to her contributions to our expansion efforts.

Next, we continue to partner with groups across the region to empower their providers to provide high-quality, value-based care. Firstly, we recently announced the acquisition of certain assets related to Texas Independent Providers, or TIP. Through its network of 120 primary care providers, TIP is expected to be an anchor for our high-quality Care Partners segment in Houston, and we expect to onboard TIP's providers onto our Care Enablement platform by the end of 2023. We are pleased that we will continue to benefit from the leadership of TIP's President Dr. Carlos Palacios, who will join ApolloMed as Chief Medical Officer for Texas to spearhead clinical initiatives for local providers, and TIP Executive Director Vincent Roth who will join us as Group Vice President of Operations for Texas and lead the continued growth and development of our Texas network.

We also announced a partnership with IntraCare to advance value-based care in Dallas/Fort Worth, El Paso, Austin and Oklahoma City. Through a network of over 425 primary care providers, IntraCare manages the care of over 40,000 members. And through this partnership, IntraCare's providers are expected to join our Care Partners business in these regions and be onboarded onto our Care Enablement platform by the end of the year. We are thrilled by the continued strong momentum we've been seeing in terms of the excitement around our Care Partners and Care Enablement offerings in both California, Texas, and beyond.

Brandon Sim: Our next strategic pillar is in empowering our Care Delivery and Care Partners providers to successfully move along the glide path towards value-based care. In California, we shared during our previous quarterly call in May that we had closed on the acquisition of For Your Benefit, or FYB, and received regulatory approval for the change in control of FYB's full-service Restricted Knox-Keene licensed health plan. We are working closely with the Department of Managed Healthcare to expand the RKK to other counties within California and to add more members within existing counties, and we believe that the process is on track relative to our expectations.

Finally, the most important strategic pillar is ensuring that we are successfully empowering our providers to deliver excellent patient outcomes, thereby managing that risk effectively. We continue to closely monitor utilization trends and did not see an increase in utilization in Q2 compared to Q1. Based on prior authorization data however, we do see a slight uptick in utilization for Q3 but do not believe this will significantly impact our overall performance or guidance for 2023.

With regards to Medicaid redetermination, a bulk of our Medicaid members in value-based arrangements reside in California, which began disenrollments in July. We have not yet seen a significant impact on either our membership or mix, but we continue to monitor and assist in the redetermination process for our members to ensure they have access to care.

With these recent developments and our solid financial performance through the first half of 2023, we are pleased to be reiterating our previously provided guidance for full-year 2023. We continue to grow membership in our core California markets and in our new Nevada and Texas geographies through organic growth, new partnerships, and inorganic activities. We continue to responsibly accelerate providers towards a value-based, aligned future. And we continue to make ongoing strategic investments in our business, our teams, and our technology, which we believe are necessary to support growth in the years to come.

With that, I'll turn it over to Chan to review our financial results.

Chan Basho: Thank you, Brandon.

We continued to deliver strong results, reporting total revenue of $348.2 million in the second quarter of 2023, a 29% increase from $269.7 million in the prior-year quarter. This was primarily driven by increased revenue from our Care Partners segment.

Chan Basho: Quickly reviewing results in each of our business segments for the second quarter versus the prior-year quarter, our Care Partners segment reported revenue of $325.2 million, an increase of 32% compared to the second quarter of 2022, primarily driven by organic membership growth in our consolidated risk-bearing entities and a more favorable payer mix. Segment operating income increased 250% to $27.8 million for the period. This was primarily driven by a larger mid-year MA risk adjustment payment this period and the retrospective trend adjustment related to the CMS DCE program in the prior-year period.

Moving to our Care Enablement segment, revenue increased 18% to $35.0 million in the second quarter of 2023. Segment operating income was $7.6 million for the period, compared to $7.3 million in the prior-year period. We continue to make investments in infrastructure, technology, and people to support our operational growth in new geographies and capabilities surrounding our RKK. We expect these investments to result in additional revenue and margin expansion over time as we onboard incremental clients.

Membership under management within our Care Enablement segment was approximately 1.3 million managed lives at the end of the second quarter ended June 30, 2023. Approximately 650,000, or half of these members, were also within our Care Partners business.

Finally, our Care Delivery segment revenue increased 14% to $26.7 million during the period. This was primarily driven by increased volume in patient visits at our primary, multi-specialty, and ancillary delivery entities. Segment operating income was $0.6 million for the period, compared to $3.4 million in the prior-year period. The decrease was a result of our ongoing investments in expanding our care delivery footprint in Nevada and Texas. As you may recall, in the past we highlighted our commitment to invest up to an incremental $10 million in 2023 to scale new geographies across all lines of business. Due to this reason, we view the results in this segment as in-line to better than guidance we provided last quarter.

In aggregate, income from operations, including corporate expenditures, was $27.0 million, an increase of 75.7% from $15.4 million in the prior-year period. Adjusted EBITDA was $35.8 million, up 44% from $24.9 million in the prior-year period.

Net income attributable to ApolloMed was $13.2 million, an increase of 10% from $12.0 million in the second quarter of 2022. Earnings per share on a diluted basis were $0.28, up 8% from $0.26 in the prior-year period.

Chan Basho: I want to note that our tax rate this quarter is 45%. Earlier this year, in my capacity as the new CFO, the finance team and I completed inventory of our tax filings, and with the assistance of outside consultants, determined we did not appropriately account for the income tax impact associated with certain intercompany dividends and also neglected to include certain loss generating entities in certain consolidated tax filing groups between 2019 and 2022. Specifically, income tax expense was appropriately accrued for the income generated by the entity that made the intercompany dividend; however, the additional tax associated with the dividend itself was not accrued. This resulted in a decrease to previously reported net income of $8 million, with a net cash impact of $7.7 million for the period 2020 to 2022. Today after the market close, we filed an 8K with additional information about the restatement. To be clear, this restatement has no impact on historically reported GAAP and non-GAAP measures, which include revenue, gross profit, pretax income from continuing operations, EBITDA, or Adjusted EBITDA. We do not believe the tax-related restatement will have any impact whatsoever on the strength of the business, our ongoing operations, our ongoing liquidity, or our need to raise capital.

Going forward, we are evaluating changes to our tax structure to reduce the current effective tax rate and amount of cash taxes. We expect to have this put into place by the fourth quarter, which we believe will result in a normalized tax rate going forward. Again, this has no impact on the measures the Company reports such as revenue, gross profit, pretax income from continuing operations, EBITDA, or Adjusted EBITDA.

Turning over to the balance sheet, we remain well capitalized and well positioned to execute on our growth initiatives. We ended the second quarter with $294 million in cash and cash equivalents, compared to $288.0 million at the end of 2022. Our working capital was $284 million, compared to $288 million at the end of 2022. Also, total debt at the end of the second quarter was $208 million.

I wanted to reiterate our 2023 outlook. We continue to be on track for total revenue between $1.3 and $1.5 billion, Adjusted EBITDA of $120 to $160 million and EPS of $0.95 to $1.20 per share. Despite the elevated tax rate for Q1 to Q3, we expect to still be within guidance for EPS, though it will most likely be in the lower half of the range.

I'd now like to turn it back to Brandon for closing comments. Brandon?

Brandon Sim: Thanks, Chan.

In closing, we are pleased with the progress we've made thus far in 2023 and look forward to taking advantage of the positive momentum we've built in the first half of the year. We believe the recent partnerships announced with a group in California, TIP, and IntraCare demonstrate the enthusiasm and need in the market for our physician-centric, value-based care platform, and we will remain laser-focused on delivering excellent growth, improving quality of care and clinical outcomes, and accomplishing those goals sustainably by continuing our strong track record of profitability.

With that, operator, let's open it up for Q&A.

Operator: Certainly. We'll be conducting a question-and-answer session. Our first question is coming from Ryan Daniels from William Blair. Your line is now live.

Jack Senft: Yeah. Hey, guys. This is Jack on for Ryan Daniels. Thanks for taking my question. First, in your prepared remarks, you noted the RKK expansion. Can you just elaborate on this and kind of what specifically this involves and then two, if you can just provide any possible timing on this expansion? Thanks.

Brandon Sim: Hey, Jack, this is Brandon. Thanks for joining the call today. I appreciate it, know it was a busy time. So with regards to your question around the Restricted Knox-Keene license, as I noted in my prepared remarks, we are working closely with the Department of Managed Healthcare in California to expand the Restricted Knox-Keene license to other counties within California. And at that point, we will be able to add more members into that Restricted Knox-Keene licensed health plan. The process includes contracting with payers and includes contracting downstream with provider groups as well as with institutional entities. And that is all a process that we believe is on track relative to our expectations.

Jack Senft: Okay, great. Thanks. As a quick follow-up, adjusted EBITDA came in sequentially better. How should we assess the quarterly cadence going forward through the rest of the year, possibly thinking about to the uptick in pre-authorizations that you noted in your prepared remarks too? How would that impact third quarter adjusted EBITDA just kind of want to make sure we're thinking about this correctly and modeling it accurately?

Chan Basho: Hey, it's Chan. Thanks so much for the question. As we think about the rest of the year, I'd say Q3 is going to be in line with Q2 and then you'll see a drop in Q4 as we've seen in historical years.

Jack Senft: Okay, perfect. Thank you. And then just one really quick final one. Can you just give us an update on the Medicaid redeterminations and kind of how that's progressed over the past few months? I think on the last call you noted that you're just starting to see some developments in May. So I'm just kind of curious how the past few months have progressed?

Brandon Sim: Hey Jack. Yeah. Definitely. So that's something we're keeping a close eye on. Almost all of our Medicaid members in value-based contracts reside in California as I noted in the prepared comments. California has been one of the slower states to start disenrollments. We started seeing that slightly in July, and it hasn't been material thus far. We've been working very closely with community groups, with payers and others to ensure that folks have access to Medicaid and access to care if they qualify and making sure they're not being disenrolled for administrative reasons. So I would say I would reiterate that there is no material impact that we're seeing yet, although we do expect that to happen perhaps in the quarter or two to come. We've accounted for that in the guidance. I mean, that's part of what Chan is talking about when he mentioned a fairly strong Q3 and a slightly weaker Q4.

Jack Senft: Awesome. Great color. Thanks, guys.

Brandon Sim: Thank you.

Operator: Thank you. Our next question is coming from Adam Ron from Bank of America. Your line is now live.

Adam Ron: Hey, guys, thanks for the question. I have a couple of questions, but on the utilization, can you provide a little bit more color around what you're seeing in terms of prior authorizations in Q3—Is that like outpatient surgery specifically, is it in MA? Just any additional color on that would be helpful.

Brandon Sim: Yeah, sure, o in Q2, so far, I know that's not the question, but in Q2 so far, we actually haven't seen a large tick up in utilization at all relative to Q1. However, reviewing the prior authorizations that are coming in, we are seeing a slight uptick in inpatient Medicare Advantage utilization. And so that's baked into some of our guidance for Q3 and Q4 coming up.

Adam Ron: All right. Makes sense. And then in terms of your normalized tax structure comment, I noticed that your tax rate is kind of higher than any other company we really cover. And I wasn't sure if that was because you were in California, but it sounds like some of it is structural that you see or that there was ways to actually reduce that. So, most of the managed care companies have been kind of hovering around mid-20s tax rate. Is that something you see as achievable or what reference would be a reasonable target?

Chan Basho: Yeah. I'd say it's closer to low- to mid-30s.

Adam Ron: Okay. And that's really the only thing driving down your net income guidance, the lower end of the range, is just higher taxes than expected for this year?

Chan Basho: That's correct.

Adam Ron: And then one of your competitors have two interesting comments, one saying that Direct Contracting was coming in better than they had expected based on data they were getting from CMS, I guess like a positive retro trend adjustment or at least relative to expectation. So is that at all factored into your guidance or results here that Direct Contracting is coming in better than expected?

Brandon Sim: For the guidance today we're not assuming any positive incremental impact for either Direct Contracting from last year or ACO REACH for this year. But that does remain a possibility, certainly. But in the spirit of conservatism, we have not accrued or incorporated any positive impact from those two programs. Again, either from a true up in 2022, which we'll know by August, or ongoing operations in ACO REACH this year into our full-year projections.

Adam Ron: But is there any data that you're getting from CMS that's like positive one way or the other or you're saying it's too early to make that call?

Brandon Sim: On the Direct Contracting entity program from 2022, we have not gotten any information from CMS that would suggest any differences relative to information we already had at the end of the year. And the final report, we do expect that to come sometime this month or early next from CMS relating to the final true up for the DCE program last year. If you're asking about the ACO REACH program for this year, we are getting monthly reports around the retroactive benchmark adjustment that has been around in line with expectations and not a noticeably positive impact.

Adam Ron: Got it. Another comment they made interesting was that they had got in discussions with payers now that the MA payers have submitted their bids for 2024, they were going to see the supplemental benefit cuts. And they said that they were larger than expected just because of the rate pressure that MA plans are seeing. And so I'm wondering, you were able to get visibility into your payer partners and what you're seeing in terms of supplemental benefit cuts for next year and how you think that will impact your numbers and if it gives you more confidence in your ability to manage through that rate headwind for next year?

Brandon Sim: Yeah. I think that's accurate on average across the board. Of course, each plan is going to look a little different, but I think on average that is also the trend that we're seeing due to their – to the payers' management of some of the risk adjustment changes, premium changes and star rating changes on their end. So I think what you're saying is accurate and we're seeing it as well. I think given the longevity of our model and the fact that we're already providing a lot of the items that may or may not have been included in supplementary benefits from some of the plans, and we're going to continue providing those services just as we always have. I think we have a good shot [at managing through the rate pressure]. We think - we expect - our model to be able to weather through that pretty consistently as we have with decades of benefit changes up and down. We haven't seen that impact our financials or our ability to deliver care at all.

Adam Ron: And then sorry for all these questions, but my last question would be one of the deals. Intracare I think it was, you mentioned 425 providers but 40,000 patients. And generally, I would think about a 60-patient panel or 100, if not over 1,000. So wondering, one, why that's a bit low for patient per provider and not sure if it's maybe like MA only or something. And then, second, if you could maybe help give context to what you think, like between these three deals that you announced in the quarter, how many patients that should add to the total number of patients and if those are all at-risk lives?

Brandon Sim: Sure. The 40,000 members are all seniors. So you're right in that the ratio of PCP to seniors is probably a bit high, relatively speaking, but the patients [seen by the provider] are not necessarily all Medicare Advantage patients. And I'm sorry, Adam, if that wasn't clear, just let me know. But in aggregate, we – it's a little early to tell exactly how many patients and the exact mix between Medicaid, commercial and Medicare Advantage, because our model does encompass and take on risk in all three areas. I would probably not want to venture a number at this point in time. But we do expect the revenue impact, I would say, to be in the tens of millions, if not higher, of impact.

Adam Ron: Great. Thank you.

Operator: {operator instructions} Thank you. Our next question is coming from Brooks O'Neil from Lake Street. Your line is now live.

Brooks O’Neil: Good afternoon, guys. I'm just curious, I think Brandon mentioned in his prepared remarks elevated risk adjustment payments. And I am just curious if you could talk about what's driving that, number one. Number two is it – do you think that trend is sustainable into the end of the year and beyond?

Brandon Sim: Thanks, Brooks, for the question. Great to hear from you. So on the elevated risk score relative to last year that drove some of the incremental outperformance for this quarter relative to same quarter last year, that was related to our efforts in more accurately capturing the chronic conditions of our senior population, which is something that we've been focused on as part of the operational and technological platform that we’ve been deploying into our provider offices over the last 12 to 24 months. As you all know, it takes quite a bit of time for risk adjustment payments to catch up with the actual act of coding the chronic condition. And so some of the results and uplift from the platform we've deployed over the past couple of years are now starting to come to bear. We also noted before that our aggregate RAF score for senior population was quite low, under 1.0. And we believed that at the time that was inappropriately low relative to the actual acuity of the chronic conditions of the patients. And so we're seeing some of that come into integration in terms of these RAF payments.

Brooks O’Neil: Do you think you can probably keep seeing additional improvements as you implement your systems, is that a fair way to characterize it?

Brandon Sim: I think related to the performance year with which these payments were related, I think that is actually it for that payment year. Of course, in future payment years we do think that there is future improvement to be had as we continue to roll out the platform to all of our providers.

Brooks O’Neil: Okay. That makes sense. Let me ask just one other one. I'm curious, Jack was asking you about the Knox-Keene license, and that's a particular fascination of mine. I was hoping you might go just a little bit deeper in talking about that, just the timing, the fact that you're on pace. But just what exactly do you think the impact of having that license will be on your business in terms of what does it mean for your provider networks, what does it mean in terms of the premium or the dollar capture you can have on a per-patient basis?

Chan Basho: Hey, Brooks, thanks so much for the question. We're very excited about our expansion of the RKK into new counties. It will allow us to quickly deploy our risk-based ecosystem into new counties as well as geographies. It will allow us to differentially capture the premium dollar as well as really expand our enablement services. In terms of timing, we are working quickly with the DMHC to expand to our current counties as well as counties where new partners are. And as you know, this is a – this takes time in terms of the regulatory efforts and we'll keep you apprised as we get further traction.

Brooks O’Neil: Great. Let me just ask one more follow-up. And I'm not trying to be too picky on this. But I'm curious. I think having that Knox-Keene license means you can accept global capitation, which would include the hospital portion and if I'm not mistaken, the premiums you've gotten historically don't include that—those hospitals, that hospital portion could potentially be quite significant for you, isn’t that true?

Chan Basho: Definitely, yes. You brought up a great point. With the RKK, we will now be able to take on the hospital risk, along with the professional risk in terms of our revenues and we’re looking forward to moving down this path. We will recognize revenues for 85-ish percent of the premium dollar versus the 35% to 40% that we are recognizing today.

Brooks O’Neil: And you think ultimately you can expand more or less for all patients that you will serve across the entire state of California, do I have that right?

Chan Basho: Yes. We will start with our Medicare Advantage population. The goal is to expand it across multiple lines of business. Of course, this does take time and it's not going to be overnight. But yes, that that is the long-term impact.

Brooks O'Neil: Cool. Thank you. I'll leave it at that. Good quarter. Good outlook. I'm excited for you guys.

Chan Basho: Thanks so much, Brooks. Great to hear you.

Brandon Sim: Thank you, Brooks.

Operator: Thank you. We reached the end of our question-and-answer session. I'd like to turn the floor back over for any further closing comments.

Brandon Sim: Thank you all for your time today. We are always open to a dialogue with investors and welcome visitors to our offices in Alhambra should any of you be in the Los Angeles area. Please feel free to reach out to us with any additional questions. We look forward to speaking to you all again on our next quarterly call. Thank you.

Operator: Thank you. That does conclude today's teleconference and webcast. You may disconnect your line at this time and have a wonderful day. We thank you for your participation today.