2022 Third Quarter Financial Results
Conference Call Transcript
November 4, 2022

Speakers:

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

Operator: Greetings and welcome to the Apollo Medical Holdings, Inc. third quarter 2022 earnings call. At this time all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. {operator instructions} I would now like to turn the conference over to your host, Carolyne Sohn, investor relations for Apollo Medical Holdings, Inc. Thank you, you may begin.

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 third quarter and nine months ended September 30, 2022, 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, 2022, continued growth, acquisition strategy, ability to deliver sustainable long-term value, ability to respond to the changing environment, operational focus, strategic growth plans and merger integration efforts, as well as the impact of the 2020 Novel Coronavirus (COVID-19) pandemic and other variants on the Company's business, operations and financial results.

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 third quarter 2022 highlights and the latest operational developments. Interim Chief Financial Officer Chan Basho will follow with a review of ApolloMed's results for the third quarter and the first nine months ended September 30, 2022. 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 of profitability driven by 40% growth on the top line in Q3, which was primarily due to increased contributions from capitated revenues. This was the result of strong organic membership growth in our core care delivery business, a more favorable membership mix, and our participation in a value-based care model for the Medicare fee-for-service population. We reported a 53% year-over-year increase in capitated revenues to $227.6 million, which accounted for nearly three-quarters of total revenue, which was $317.0 million for the quarter.

Before we get into the quarter, I want to highlight a very important fact that sets ApolloMed apart from other providers. It's our desire to serve our entire communities across all payer types: that is, Original Medicare, Medicare Advantage, Medicaid, and Commercial patients, and support them across their entire lives. Our willingness and dedication to serving all members of our communities, and the unique care model and value-based care infrastructure we have built in order to do so successfully, makes us an extremely valuable partner to payers and providers. It has also fueled our ability to consistently grow the business profitably, which drives a virtuous cycle as we continue to invest in the long-term health and wellness of the communities we serve and expand our care delivery model

into new communities across the country. We believe that the foundational tenet upon which successful healthcare delivery is built is the trusted relationship between a patient and their provider, and we will continue to invest in that sacred relationship in order to effect industry-leading clinical outcomes for our patients.

Brandon Sim: Going back to the financials, our operating expenses during the third quarter increased by $93.0 million, or 53%, primarily due to a return of pre-COVID medical expense run rates and growth in membership, which is in line with the increase in capitated revenues. As discussed on our last quarterly call, we continued to see an increase in MLR compared to that in 2021, primarily as a result of utilization returning to pre-COVID levels.

Despite the increased opex, we reported $26.0 million in net income attributable to ApolloMed shareholders and GAAP earnings per share on a diluted basis of $0.56 for the quarter. Adjusted EBITDA was $57.1 million, compared to $62.9 million in Q3 of last year.

I am excited to announce that we are raising our revenue, net income and EBITDA guidance for full-year 2022 as a result of our strong performance in the first three quarters of the year. We are reiterating guidance for Adjusted EBITDA because we have revised our Adjusted EBITDA calculation beginning this quarter to exclude addbacks for provider bonus payments and losses from recently acquired IPAs. We strive to ensure that our shareholders better understand the clinical and financial outcomes generated by our unique model, and removing these addbacks will bring Adjusted EBITDA closer to free cash flow and highlight the unique level of profitability that our model generates as it grows 40% same quarter year over year.

In summary, our revenue forecast for the full year is increasing from a range of $1.055 to $1.085 billion to a new range of $1.095 to $1.115 billion. Our net income forecast for the full year is increasing from $38 to $57 million to a new range of $50.5 to $67 million and our EBITDA forecast is increasing from a range of $81 to $111 million to a new range of $107.5 to $133.5 million. And despite the revised Adjusted EBITDA calculation in which we're removing the addbacks related to one-time provider bonuses and losses due to recent growth, we are maintaining our Adjusted EBITDA guidance of $136 to $166 million. Prior to this calculation adjustment, we had expected to beat this range. With the new calculation, we still anticipate being within this range but on the lower end. For future years, we continue to anticipate to grow at a 30% revenue growth clip year over year with a target EBITDA margin of 10-15%.

Moving to recent operational developments, we made a couple of very exciting announcements a few weeks ago. We are pleased to have closed on the acquisition of nine primary care clinics in Las Vegas, Houston, and Fort Worth operating as Valley Oaks Medical Group, in mid-October. This

marks our official expansion into the Nevada and Texas markets, and we look forward to delivering positive clinical outcomes and improved care experiences to the underserved patients in these local communities through our unique care model. We have talked about making bigger moves into new geographies, and we are thrilled to begin building trusted relationships with patients and communities in Nevada and Texas.

Brandon Sim: In late September, we announced the signing of a definitive agreement to acquire 100% of the fully diluted capitalization of All American Medical Group, or AAMG, and For Your Benefit, or FYB, as well as certain related managed care assets. AAMG is a physician group in the San Francisco Bay Area, and FYB is affiliated with AAMG and is licensed by the California Department of Managed Health Care as a full-service Restricted Knox-Keene licensed health plan. We closed on the acquisition of AAMG on October 31st and expect to complete the remaining transactions by the end of the first quarter of 2023 pending regulatory approval.

The Restricted Knox-Keene license that is a part of the FYB transaction will allow us to assume full financial responsibility, including both professional and institutional risk, for the medical costs of its members. This means that, for the first time, ApolloMed will be able to recognize a much larger percentage of the premium dollar as revenue for its managed care risk-bearing members in California. Instead of recognizing only 40-45 cents of each premium dollar for taking on professional risk, we will now be able to recognize closer to 85 cents, illustratively, of the premium dollar for taking on both professional and institutional risk, or global risk, in capitated revenues. Today, we are currently taking on facility risk by partnering with hospitals or payers where we recognize shared savings and incentive revenue, and we will translate the success we have achieved in doing so to better coordinate care for our members in the future via the Restricted Knox-Keene license.

We view this as a significant opportunity for both revenue and EBITDA, but we do want to note that we anticipate the process of assuming this risk level across all of our members to be a gradual process.

The AAMG-FYB investment and partnership will also add over 250 physicians to ApolloMed's network of providers and over 15,000 Medicare Advantage, Commercial, and Medicaid patients in the City and County of San Francisco and in San Mateo County. We are thrilled to be expanding upon our presence in Northern California following the acquisitions of Access Primary Care Medical Group and Jade Health Care Medical Group in the past year. With the addition of AAMG and FYB to the ApolloMed family, we will now serve over 30,000 patients in the San Francisco Bay Area.

Brandon Sim: In the remainder of 2022, we look to continue strengthening our foothold in our core California markets while continuing to build rapidly in newer markets such as New York, Nevada and Texas. As we continue to empower our physicians to deliver exceptional clinical outcomes, we believe there is a great deal of runway for our unique value-based care and value-based enablement offerings.

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 $317.0 million in the third quarter of 2022, a 40% increase from $227.1 million in the prior-year quarter. This was primarily driven by increased capitation revenue resulting from organic membership growth in our core IPAs and participation in a value-based Medicare fee-for-service model.

Capitation revenue increased 53% to $227.6 million during the period, accounting for 72% of total revenue for the quarter ended September 30, 2022.

Risk pool settlements and incentives revenue increased 8% to $64.8 million during the period, from $59.9 million in the prior-year period, primarily driven by a $27.0 million increase in the shared savings settlement earned from Apollo's participation in an ACO related to the 2021 performance year. This was partially offset by reduced risk pool payments due to an increase in utilization post the COVID-19 public health emergency period.

Fee-for-service revenue increased 77% to $12.9 million, from $7.3 million in the prior-year quarter. The increase was primarily due to a $4.0 million increase from the consolidation of Sun Labs beginning August 2021 and DMG beginning October 2021, as well as increased visits to our surgery center.

Our membership remained at approximately 1.2 million managed lives at the end of the third quarter ended September 30, 2022. Approximately 600,000, or half of our members, were under capitated risk-bearing arrangements through our consolidated IPAs.

Total operating expenses increased about 53% to $266.9 million in the third quarter of 2022, from $174.0 million in the prior-year period. This was primarily a result of increased cost of services due to a return to pre-COVID-19 medical expense run rates and growth in membership, which was commensurate with our increase in capitation revenue.

Net income attributable to ApolloMed was $26.0 million, compared to $34.3 million in the third quarter of 2021. Earnings per share on a diluted basis were $0.56, compared to $0.74 in the prior-year period, mainly due to the increase in operating expenses mentioned earlier.

Chan Basho: We reported EBITDA of $48.2 million in the third quarter of 2022, which compares to negative EBITDA of $0.3 million in the prior-year period. Adjusted EBITDA was $57.1 million, compared to $62.9 million in the prior-year period. We place greater emphasis on the Adjusted EBITDA figures as these numbers back out the impact of excluded assets, stock-based compensation, other income, and income from equity method investments. The Adjusted EBITDA figure for Q3 2022 takes into account a significantly lower non-cash unrealized loss of $3.9 million as a result of a decrease in fair value associated to the passive investment in a payer partner's shares held as marketable securities and other investments, which compares to $69.2 *[correction: $62.9]* million in unrealized losses as a result of a 1-to-3 conversion of a payer partner's preferred shares to common stock in the prior-year period. As a reminder, these payer partner shares are in the excluded assets bucket that we've described in the past as they solely benefit our affiliate APC and its shareholders.

With that, I'll go over a few financial highlights for the nine months ended September 31, *[sic]* 2022.

Total revenue was $850.0 million, up 47% from $578.8 million in the prior-year period, primarily attributable to organic growth of membership and participation in a value-based fee-for-service model. Total operating expenses increased to $758.3 million, from $482.9 million in the prior-year period, primarily due to an expected return to pre-COVID-19 medical expense run rates and growth in membership, which was commensurate to our increase in revenue.

Net income attributable to ApolloMed was $51.6 million for the nine months ended September 30, 2022, compared to $60.1 million for the nine months ended September 30, 2021. Diluted EPS was $1.12 for the nine months ended September 30, 2022, compared to $1.33 in the prior-year period.

Turning over to the balance sheet, we remain well capitalized and well positioned to execute on our growth initiatives. We ended the third quarter with $184.0 million in cash and cash equivalents, compared to $233.1 million at the end of 2021. Our working capital was $287.4 million, compared to $283.4 million at the end of 2021. Total stockholders' equity increased to $513.5 million at September 30, 2022, from $460.5 million at December 31, 2021.

Total debt at the end of the third quarter was $205.9 million.

I'd now like to turn it back to Brandon for a discussion of our growth strategy and outlook for the remainder of 2022. Brandon?

Brandon Sim: Thanks, Chan.

We expect to close out 2022 on a strong note. The Valley Oaks and AAMG-FYB transactions represent several of the growth levers we have discussed in the past—geographic expansion of our care delivery model and increasing the amount of risk we can take via the Restricted Knox-Keene license. We are working closely with the FYB team to complete this transaction and believe these investments will continue to drive strong growth in revenue and EBITDA.

We also continue to be in active discussions with provider groups and healthcare organizations all over the country, and we continue to be energized by the amount of enthusiasm we are seeing from physicians about our unique physician enablement model and technology platform.

As I noted earlier, I'm excited to that we are able to raise our previously disclosed guidance projections for revenue, net income and EBITDA for the full year of 2022. We are maintaining our guidance for Adjusted EBITDA for the year given the aforementioned revisions to our Adjusted EBITDA calculation. We have shared these details on slide 11 of our earnings supplement.

Please keep in mind that the net income and EBITDA guidance do take into account the potential impact of APC's passive investment in a payer partner, which Chan also mentioned in his comments earlier. For this reason, we place greater emphasis on the net income attributable to ApolloMed shareholders and Adjusted EBITDA metrics. As any material developments arise, we will be sure to update the markets and re-evaluate guidance as appropriate.

In closing, we have made investments thus far in 2022 in our people, technology, and communities in order to give us strong visibility into an exciting 2023 and beyond. We continue to prioritize the foundational trust that patients have in us and our providers, and we will continue to invest in the long-term health of our communities. Together, I am confident that we will transform the way healthcare is delivered across the country, accelerating our healthcare system towards a future in which all Americans, regardless of age, race, circumstance, or socioeconomic status have access to a high-quality healthcare experience.

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

Operator: Thank you. At this time, we will be conducting a question-and-answer session. {operator instructions} Our first question comes from the line of Ryan Daniels with William Blair. Please proceed with your question.

Ryan Daniels: Yeah, thanks for taking the question, and congrats on the quarter. Brandon, can you talk a little more about the RKK process and how quickly

you'll be able to transition to more of a full risk model and the $0.85 on the dollar? Is that something that you'll go through kind of over a 3-4 year period as you contract renew with the managed care plans? Thanks.

Brandon Sim: Good morning, Ryan. Thank you for joining us. Great to hear from you. You're absolutely correct. It's not going to be an instant process. We anticipate having regulatory approval from the Department of Managed Health Care in California sometime in Q1 of next year. We'll certainly update the investor base when that happens, but afterwards, there is a fairly lengthy process of re-contracting across all of our 20+ payers, hospital partners, so on and so forth in order to make sure that all of our patients are covered under the Restricted Knox-Keene license. I would probably guide for a fairly large range of 2-4 years for everyone to be in that higher risk track across the board.

Ryan Daniels: That makes sense. And then, ahead of and during that process, are there incremental technology investments that you need to make to the platform as you take on more institutional risk or are you already kind of deploying those models to ensure the shared savings in the risk pool line such that you don't have to make a ton of investments to move to that risk level?

Brandon Sim: Yeah, thanks, Ryan. So I think there are going to be a few investments on the technology as well as the clinical side to ensure that we have all the risk controls in place to take on global risk in all of the new geographic regions that we've entered. We're very used to doing that, and you can see the results of that in the shared risk pool and settlements line item historically. But especially as we move into new geographies, there will be a little bit of investment required on the clinical side to make sure everything continues to run as smoothly we have run it in the past. But we don't anticipate it to be a very large investment that we'll have to make given our historic ability to take on global risk successfully.

Ryan Daniels: OK great. And then a couple questions on kind of the core California Medicaid business. Obviously some new awards there in counties in which you participate. I assume you already have relationships with, you know, all or some of the winners of those contracts so 1) is that the case and 2) if not, do you envision any turnover in your membership base of capitated risk with Managed Medicaid plans or do you think you can kind of re-contract with new winners and keep that intact over time?

Brandon Sim: Yeah, absolutely. That's one of the beauties of the model that we have, which is we're payer-agnostic so we have contracts with all of the large winners of the re-bid process of Medicaid in California. We already have members with them, so if members were to move from one of the losers for example to a payer who had won a new contract in the county, we wouldn't anticipate any disruptions in care for those patients.

Ryan Daniels: OK perfect and then my final question, any thoughts on Medicaid redetermination? It sounds like all else equal that will probably start to begin end of January, early February. I know states have effectively a year to go through that, but do you envision that having a big impact on that book of business? I know California Medicaid is an extremely low payer so maybe even if you lose lives there, you can just absorb that with growth with a much smaller amount of Medicare Advantage lives. But any thoughts there would be helpful, thank you.

Brandon Sim: Absolutely. We're still on the lookout for when the public health emergency will end and that redetermination will happen. We anticipate the impact to be somewhere between 5-15% of our Medicaid book of business potentially. Of course we're working very hard to make sure everyone is enrolling as necessary so they don't experience any disruptions in their care, and we do anticipate that some of them will unfortunately not be re-enrolled properly. So we probably anticipate mid-, single-digit percentage attrition in Medicaid, Medicaid book of business. As you mentioned, it's not quite as high in terms of PMPM and probably would be absorbed. We don't anticipate there being a material impact to overall financials due to the redetermination. But we are making sure that people continue to have access to care.

Ryan Daniels: OK, thank you for that. And I also applaud the new EBITDA calculation. I think it's a lot more consistent with how people look at the model and your cash flow. So I appreciate that. Thanks, guys. Have a good day.

Brandon Sim: Absolutely. Thank you, take care.

Operator: Thank you. {operator instructions} Our next question comes from the line of Sarah James with Barclays. Please proceed with your question.

Sarah James: Thank you. Congrats on a great quarter, and I echo the sentiment. I think the switch in accounting policy is going to make it a lot easier to compare you to your peer group. So I just wanted to unpack a little bit of what's happening in the risk pool and incentives line. You know, if we look at kind of the core of that with your settlements with hospital partners, how did that trend this year versus 3Q'21? Because I know last year you had that benefit from low COVID utilization. So how's that looking for you guys? Are you back to a normal run rate level or are you still getting some benefit from low utilization on that line?

Brandon Sim: Hey, good morning, Sarah. It's good to hear from you. Thanks for the question. Yeah, so we are seeing MLRs this quarter that are back to normal. We don't anticipate any future increases in MLR in our core business. That has stabilized kind of in the low to mid-80s in MLR across all of our businesses, both in the core and in new which are kind of lumped together in new accounting policies. As for how that impacted the risk pool and incentives line item this year, as we have disclosed, the

shared savings payments were $29.0 *[correction: $27.0]* million higher than it was same quarter last year. The shared savings from our hospital partners was down around $25 million YTD. We don't anticipate—there are no more COVID tailwinds baked into that hospital payer partner so far and we don't anticipate there to be any in our guidance in the future either.

Sarah James: Great. Can you help us understand what the thresholds or benchmarks are for those hospital bonuses? What types of metrics are you being evaluated on and how are you falling in the range versus, you know, fee escalation there?

Brandon Sim: Right. So for hospital payer partners, it's a pretty simple arrangement actually. They receive capitated dollars as a percentage of premium for each member that they have on a PMPM basis, and we essentially charge all facility cost against that capitated pool. Whatever is left we will split some percentage to the hospital and some percentage to us. So those arrangements range from us keeping 50% of the excess surplus in that pool to perhaps 80% in some of our contracts. So that's essentially the only metric that is measured, it's just however much is left in the risk pool we are splitting that amount in a predetermined fashion. Of course those are correlated to clinical measures that we are monitoring very carefully all the time in terms of our in-patient bed days, readmissions, and so on and so forth. We've seen those numbers stabilize as well in a post-COVID world, as much as that can happen.

Sarah James: Great. And last question is, if you can just refresh us on how you view organic growth. You know, you guys have branched out geographically, I think, since you last guided on that. So how are you thinking about organic growth these days?

Brandon Sim: Yeah, absolutely. So we-- as you know we've raised guidance for revenue this year. We continue to see strong growth even throughout the year. Of course it is AEP now so we will anticipate to see kind of more chunky growth in Q1 of next year. But that being said, we are still guiding towards mid-kind of teens organic growth, kind of look forward to making sure that our new investments in new geographies are contributing much more rapidly to that overall book of business. That being said, I would temper expectations slightly by saying that in other states that we've entered such as Nevada and Texas we are not yet in fully capitated global risk arrangements the way that we are used to doing in California. Some of that book of business is still fee-for-service for example, so over the next two years, 18 months we would work to ensure that the model aligns from a reimbursement perspective more similarly with what we've had historically in California. But we view those as kind of opportunities and tailwinds to increase revenue in some of these other states that we've entered.

Sarah James: Great. Thank you.

Brandon Sim: Thank you so much, Sarah.

Operator: Thank you. Ladies and gentlemen, that concludes our question-and-answer session. I'll turn the floor back to management for any final comments.

Brandon Sim: Well, thank you all for attending the earnings call today. Thank you for your time. We are always open to a dialogue with investors and would welcome any of you to our offices in Alhambra should any of you be in the Los Angeles area. Please feel free to reach out to us or our investor relations firm The Equity Group with any additional questions. We look forward to speaking to you all again on our next quarterly call. Thank you so much. Have a great day.

Operator: Thank you. This concludes today's conference call. You may disconnect your lines at this time. Thank you for your participation.