PARTICIPANTS

Corporate Participants

Crissy Buchanan Carlisle – Chief Investor Relations Officer, Encompass Health Corp.
Mark J. Tarr – President, Chief Executive Officer & Director, Encompass Health Corp.
Douglas E. Coltharp – Executive Vice President & Chief Financial Officer, Encompass Health Corp.
April K. Anthony – Chief Executive Officer-Home Health and Hospice, Encompass Health Corp.
Barbara A. Jacobsmeyer – Executive Vice President & President-Inpatient Hospitals, Encompass Health Corp.

Other Participants

Whit Mayo – Analyst, UBS Securities LLC
Brian Gil Tanquilut – Analyst, Jefferies LLC
A.J. Rice – Analyst, Credit Suisse Securities (USA) LLC
Matt Larew – Analyst, William Blair & Co. LLC
Joanna Gajuk – Analyst, BofA Securities, Inc.
Frank George Morgan – Analyst, RBC Capital Markets LLC
Andrew Mok – Analyst, Barclays Capital, Inc.
Pito Chickering – Analyst, Deutsche Bank Securities, Inc.
Scott J. Fidel – Analyst, Stephens, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to Encompass Health's Fourth Quarter 2020 Earnings Conference Call. At this time, I would like to inform all participants that their lines will be in a listen-only mode. After the speakers' remarks, there will be a question-and-answer period. [Operator Instructions] Today's conference call is being recorded. If you have any objections, you may disconnect at this time.

I'll now turn the call over to Crissy Carlisle, Encompass Health's Chief Investor Relations Officer.

Crissy Buchanan Carlisle, Chief Investor Relations Officer, Encompass Health Corp.

Thank you, operator, and good morning, everyone. Thank you for joining Encompass Health's fourth quarter 2020 earnings call. With me on the call today are Mark Tarr, President and Chief Executive Officer; Doug Coltharp, Chief Financial Officer; Barb Jacobsmeyer, President, Inpatient Rehabilitation Hospitals; April Anthony, Chief Executive Officer of Encompass Home Health and Hospice; and Patrick Darby, General Counsel and Corporate Secretary.

Before we begin, if you do not already have a copy, the fourth quarter earnings release, supplemental information and related Form 8-K filed with the SEC are available on our website at encompasshealth.com. On page 2 of the supplemental information, you will find the Safe Harbor statements, which are also set forth in greater detail on the last page of the earnings release.

During the call, we will make forward-looking statements, which are subject to risk and uncertainties, many of which are beyond our control. Certain risk and uncertainties, like those relating to our ongoing strategic review and its impact on our business and stockholder value as well as the magnitude and impact of COVID-19 that could cause actual results to differ materially

from our projections, estimates and expectations are discussed in the company's SEC filings, including the earnings release and related Form 8-K and the Form 10-K for the year ended December 31, 2020 when filed. We encourage you to read them.

You are cautioned not to place undue reliance on the estimates, projections, guidance and other forward-looking information presented, which are based on current estimates of future events and speak only as of today. We do not undertake a duty to update these forward-looking statements.

Our supplemental information and discussion on this call will include certain non-GAAP financial measures. For such measures, reconciliation to the most directly comparable GAAP measure is available at the end of the supplemental information and at the end of the earnings release and as part of the Form 8-K filed yesterday with the SEC, all of which are available on our website.

I would like to remind everyone that we will adhere to the one question and one follow-up question rule to allow everyone to submit a question. If you have additional questions, please feel free to put yourself back in the queue.

But before I turn it over to Mark, I want to reiterate that the strategic review for our home health and hospice segment is ongoing. Our board of directors has made no decision. Accordingly, our 2021 guidance and our longer-term growth targets assume the continuation of the current structure of our business. The guidance and growth targets may change depending on the ultimate outcome of the review. Additionally, because the strategic review is ongoing, we will not be able to comment further on it today.

With that, I'll turn the call over to Mark.

Mark J. Tarr, President, Chief Executive Officer & Director, Encompass Health Corp.

Well, good morning, everyone, and thank you, Crissy. We have a history of adapting to change and doing it well. Looking back on 2020, I'm proud of our company and how we responded to the changes going on in the world around us. Both of our business segments quickly responded to meet the needs of our patients, our employees and our business partners. The patient experience has always been at the center of what we do. This year, in particular, the impact of our caring and compassionate teams has been on full display. As our hospitals were forced to close their doors to visitors and as our homebound seniors were isolated from family and friends, often the only direct contact patients had for weeks at a time were their Encompass Health clinicians. I've heard countless stories of how our staff kept patients connected to loved ones and showed them the kind-hearted care they so deserved. COVID-19 shut most of the world down, our employees came to work putting the well-being of our patients first; they truly are heroes.

Turning to the performance of both of our segments in 2020. Our inpatient rehabilitation segment opened four new hospitals and expanded existing hospitals by 117 beds. They successfully responded to regulatory changes impacting our reimbursement, achieving better than initially expected pricing and continued to demonstrate our value proposition to Medicare Advantage payers with Medicare Advantage discharges increasing 34% year-over-year. We also continued to develop and implement post-acute solutions. We fully deployed our proprietary readmission prevention model. This program uses predictive analytics to determine the risk of a patient's readmitting after they discharge from an Encompass Health hospital. In our pilot market, use of this tool lowered the 30-day readmission rate by 280 basis points. So, we're excited how this tool further enhances our value proposition to healthcare providers and payers. In addition, we deployed a home health agency quality reporting tool and began development of a SNF quality reporting tool to ensure we're accessing the highest quality clinical partners and for building preferred provider networks in all of our markets.

In addition, we expanded our proprietary marketing tool known as the post-acute care strategic analysis or PACSA to include DRG level information on cost and quality to enhance our conversations with providers and payers. In our home health and hospice segment, we once again delivered industry-leading margins in spite of the pressures brought on by PDGM rate changes and COVID-related challenges. In the fourth quarter of the year, we exceeded our prior-year adjusted EBITDA margin by 250 basis points. This strong margin resulted from the effective management of our field clinicians via our new therapy compensation model and our continuous focus on productivity. The effective management of our patient care plans supported by the Medalogix CARE Tool and the effective management of our spending on routine administrative costs.

Both of our segments continue their focus on clinical collaboration. Our Medicare clinical collaboration rate is over 43%, and our Medicare Advantage rate increased to over 15% in 2020. Additionally, in the fourth quarter, we executed a new national contract with UnitedHealthcare for our home health service line that will bolster not only our clinical collaboration opportunity for Medicare Advantage patients, but will also produce a new avenue for referral growth. We have a lot to be excited about as we enter 2021.

Our inpatient rehabilitation segment is well-positioned as the market leader and is ready to meet the increasing demand of their growing senior population. From 2010 to 2018, the supply of IRFs remained relatively stable, yet the 65-plus population grew 32%. There's a supply and demand imbalance, and we're one of the few companies with both the operational expertise and capital necessary to build and operate freestanding IRFs. We have eight new hospitals expected to open in 2021, and we expect to add 100 to 150 beds to existing hospitals. We'll also continue development on the 10 new hospitals we expect to open in 2022. We have a robust development pipeline and we expect more growth-related announcements throughout the year. We will continue to educate stakeholders about the value proposition of our inpatient rehabilitation hospitals. We'll continue to use data to show our outcomes and total episodic costs to healthcare providers and payers demonstrating that we are the high quality, cost-effective provider they want and need. Specifically, we plan to build on momentum we had in 2020 with Medicare Advantage by focusing on getting more one-on-one meetings with local and regional MA medical directors who heavily influenced the preauthorization process. We also will remain focused on developing and implementing post-acute solutions.

Our robust technology capabilities, including the use of predictive data analytics, differentiate us from our competitors. In 2021, we'll monitor the data from the readmission prevention model we deployed in 2020, and we'll develop and pilot a fall prevention model specific to inpatient rehabilitation. Our strategic sponsorship of the American Heart Association/American Stroke Association is continuing. In 2021, we plan to co-brand and launch stroke continuing education programs for healthcare providers. As part of our education efforts for patients and families on the importance of inpatient rehabilitation after a stroke, we are featuring Encompass Health patient success stories on the association support network blog and launching how to videos to assist stroke survivors with completing daily activities.

Let's talk now why we're excited about home health and hospice: a strong demographic tailwind, a strong and increasing patient preference for in-homecare, a growing number of seniors experiencing four or more chronic conditions and the cost-effectiveness of treating those conditions in the home, reimbursement visibility that's better than we've seen in a decade, and accelerating opportunities for market share capture both organically and through industry consolidation. As you may recall in December, we announced we are exploring strategic alternatives for our home health and hospice business. Being one of the top providers in the nation as measured by both our financial results and our quality outcomes allows us to consider a wide array of transactions and structures. Our strategic review is ongoing and no timetable has been established for its completion. So, we remain focused on the diligent execution of our strategy for both segments. In 2021, we look forward to the full return of elective procedures and the resulting growth it will produce for our home health service line. We also look forward to the continuation of the strong

admission trends we've experienced in hospice. In addition, we believe there is strong interest in partnering with Encompass Home Health among accountable care organizations and Medicare Advantage payers seeking value-based payment arrangements. Over the past few years, we have participated in various ACO arrangements where we've demonstrated our value through the achievement of savings for these organizations. We'll continue to build and rely upon these experiences to become even more innovated in the way we work with Medicare Advantage payers. Our goal here is simple: to deliver higher quality outcomes for their members and better share financial outcomes for our organizations and their plans. With the combination of the industry-leading readmission rates resulting in more healthy days at home for our patients, success and prior risk-based payment arrangements and a commitment to scale and density at the regional level, Encompass Health is the clear choice for organizations engaged in risk-based payment models for America's seniors.

Operationally, we're excited about the full deployment of the Metalogix care module and the further improvements it will produce in both quality outcomes and our operating margins. This tool assists us in ensuring our patients have a care plan that includes the right number of visits performed by the right level of staff at the right time to achieve the desired outcome. We're also collaborating with two homecare organizations that provide personal care to support a SNF-at-home program in order to meet a growing need for these services in our markets. Additionally, we're rolling out a virtual visit platform with a national payers' capitated program. This virtual platform app allows patients to participate in a secure video call via a personal device such as smartphone, tablet or computer with their physician, nurse, care manager or other medical staff.

As we look ahead into 2021, we are confident the fundamentals of our business are intact and strong. In fact, we believe COVID-19 has created an even stronger awareness of the high level of care we provide in our inpatient rehabilitation hospitals and further reinforce home as a preferred care setting. We expect stakeholders will increasingly divert admissions away from SNFs to higher-value IRFs and homecare providers. And as the population ages, the demand for our high-quality services will increase.

Our initial guidance for 2021 includes consolidated net operating revenues of $5 billion to $5.17 billion, consolidated adjusted EBITDA of $925 million to $955 million, and an adjusted earnings per share of $3.31 to $3.53. We remain confident in the long-term prospects for both of our business segments. Yesterday, we issued longer-term growth targets for our company, which you can see on page 16 of the supplemental information that accompanied our earnings release. This outlook included an 8% to 10% CAGR for consolidated net operating revenues, an 8% to 10% CAGR for consolidated adjusted EBITDA, and a 5% to 7% CAGR for adjusted free cash flow. These targets are supported by our strong financial foundation and the substantial investments we've made and we'll continue to make in our businesses. We feel very good about the strength of our organization, its team and the opportunities that lie before us.

Now, with that, I'll turn it over to Doug.

Douglas E. Coltharp, Executive Vice President & Chief Financial Officer, Encompass Health Corp.

Thanks, Mark. And good morning, everyone. As Mark stated, we're pleased with the performance of both of our segments. We exited the year on a positive note with fourth quarter consolidated net operating revenues up 2.5%, consolidated adjusted EBITDA up 0.7%, and adjusted EPS up 9.4%. And we continue to generate high levels of free cash flow with adjusted free cash flow increasing 55.6% in the quarter, and 12.3% for the year. In our inpatient rehabilitation segment, our revenue per discharge was higher in 2020 than initially expected primarily due to the higher acuity of our patients throughout the year as well as the suspension of sequestration that began May 1.

Inpatient rehabilitation volumes started 2020 strong before being significantly impacted beginning in March. Patient expenses recovered substantially in the second half of 2020 returning to 2019 levels or higher. However, as we've discussed previously, we experienced an increase in our average length of stay which resulted in a year-over-year decrease in discharges and EBITDA margin. Specific to the fourth quarter of 2020, revenue in our inpatient rehabilitation segment increased 4.1% compared to 2019 driven by pricing. Growth in revenue per discharge primarily resulted from a higher acuity patient mix, an increase in reimbursement rates, and the suspension of sequestration. Adjusted EBITDA decreased 3.2% in the fourth quarter of 2020 compared to 2019 primarily due to increases in bad debt expense, group medical expense, and use and cost of PPE. In the fourth quarter of 2020, we performed a review of our accounts receivable balances and related reserves that resulted in a $4.5 million increase to bad debt primarily related to prior-period denied claims. Our bad debt expense for full-year 2020 was 1.6% within the initial guidance range we provided for the year, and we expect bad debt to be in a range of 1.4% to 1.6% for 2021.

Turning now to our home health and hospice segment. Our home health line of business also came out of the gate strong in 2020, with starts of episodes for January and February up 8.5%. Limitations on elective procedures, senior living and skilled nursing facility access restrictions and COVID surges in states where we have market concentrations limited our growth in 2020. We exited the year with starts of episodes of 2.2% over prior-year levels, in spite of the fact that our admissions during the quarter declined 27% from senior living facilities, 36% from skilled nursing facilities and 12% from patients receiving elective procedures in acute care hospitals. In addition, there were an average 360 employees per day on COVID-related quarantine during the fourth quarter, which represented a 48% increase over the third-quarter average and further impacted our ability to confer referrals into admissions.

Our home health team continued to manage costs well contributing to fourth quarter adjusted EBITDA growth of 11.9% over the prior year. Our cost per visit was down almost 4% with the primary driver of this improvement being the compensation structure changes we made in May 2020 coupled with the productivity of our full-time staff. As we start 2021, we believe our return to volume growth in both segments involves return of orthopedic and lower extremity joint replacement cases, and mitigation of COVID-related isolations and quarantines. As discussed, many of our markets continue to have limited elective surgeries, particularly with elderly patients with complex medical conditions.

In 2020, our IRFs treated approximately 4,500 fewer orthopedic and lower extremity joint replacement patients than we did in 2019, and our home health agencies treated approximately 3,100 fewer. With regard to isolations and quarantines, at any given time, 10 to 15 of our hospitals were impacted in the fourth quarter of 2020 by [ph] Center's caps (22:34) due to isolation needs for patients with COVID and/or staffing constraints due to quarantines. In January 2021, that number increased to approximately 30 hospitals. In the fourth quarter of 2020, approximately 360 of our home health and hospice employees were quarantined on average at any given time. That number increased to almost 500 per day in January. The rollout of the vaccine will assist in addressing all of these issues. And accordingly, we expect volumes to increase more significantly beginning in the second half of 2021.

In addition to the vaccine, revised CDC guidelines and expedited COVID testing results will assist with reducing the number of days an individual must quarantine. In the fourth quarter of 2020, we had 30 hospitals with a rapid testing device and we expanded that to 70 hospitals in January 2021. Our hospitals and homecare agencies using offsite testing are experiencing improved turnaround times. So, we believe we will see a reduced capacity and staffing constraints across all of our service lines.

[indiscernible] (00:23:54) to our IRF segment, we expect the acuity of our patients to remain elevated through at least the first half of 2021 and to begin normalizing thereafter. With regard to expenses, we will continue to focus on managing staffing levels to volumes. We did provide wage

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increases to our hospital employees effective October 1, 2020 at the same time when we received our fiscal year Medicare price increase of 2.3%. We expect benefit costs to increase 5% to 8% in 2021 due to general inflationary increases as well as the rebound of employee deferred medical visits and procedures. While we do not expect our PPE pricing to return to pre-COVID levels, we do expect the higher cost we saw in 2020 to subside as allocations from primary lower-price vendors continue to increase. We expect utilization of PPE to remain elevated as precautions continue throughout 2021. We will also incur $15 million to $20 million of preopening and ramp-up costs associated with new hospitals as our development activities continue to accelerate. In our home health and hospice segment, our primary focus in 2021 is on increasing institutional and early admissions with the return of elective procedures and the expected normalization of the mix of patients. We expect to maintain the savings realized from the compensation structure changes enacted in 2020. However, we anticipate the nursing staff challenges across the country will lead to increased compensation rates for the home health nursing discipline, which comprises approximately 44% of our total visit volume. We expect to mitigate a portion of these increases through LPN optimization and the improved care planning that will be supported by the Medalogix CARE Tool.

As Mark stated earlier, we've reinstated longer-term growth targets for our company, and we believe we have the capital structure to support the investments in our growth. We are fortunate that one of the characteristics of our business model is that we generate consistently high levels of free cash flow. Our 5% to 7% adjusted free cash flow CAGR target over the next five years is off of a high base year in 2020 and reinforces our confidence in our expected free cash flow. Our net leverage was a very manageable 3.6 times at year-end and our debt maturities are well-spaced. We are well-positioned financially and operationally for the future.

With that, operator, we'll open the lines for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Whit Mayo of UBS.

<A – Mark Tarr – Encompass Health Corp.>: Hello, Whit.

<A – Doug Coltharp – Encompass Health Corp.>: Hello, Whit.

<Q – Whit Mayo – UBS Securities LLC>: Hey. Thanks. I really just have one question for right now, and when I look at the performance of the home health business in the fourth quarter, I mean it seems like EBITDA now is tracking above my pre-COVID forecast for the fourth quarter growing up 11% year-over-year. And it feels like there's some momentum coming into 2021 when I look at the cost per visit you're tracking significantly below first-half levels, which would seem to imply some noticeable tailwinds coming into 2021. So, how are you thinking about the direction of those trends? And then, if you could maybe comment a little bit more on the visits per episode and some of the initiatives you may have in the field and how that could trend. It just feels like there perhaps is a little bit of a disconnect between the near-term performance versus what may be implied within the full-year range? Thanks.

<A – Mark Tarr – Encompass Health Corp.>: Whit, I'll ask April to give her insights on that.

<A – April Anthony – Encompass Health Corp.>: Sure. So, Whit, certainly appreciate the perspectives, and we are pretty encouraged about what we're seeing on the volume side as Doug mentioned, if you look at the December trending, we continue to trend in the right direction from a volume perspective and in spite of shifts as we mentioned in our SNFs and our senior living patients as well as the electives, I think our team has done a really good job of replacing that volume with other sources. And so, we're obviously encouraged about that and believe that once some of the COVID pressures release that some of the historical referral sources will return to us. We think all of the impact are very COVID-driven and relatively short-lived. We're also encouraged, as Doug mentioned, about our cost per visit and feel like the compensation structure changes that we made back in May have served us well in the third and fourth quarter, and we see the continuing opportunity there. But we are concerned about costs per visit in the nursing discipline and the financial shortage that exists that has just been exacerbated by COVID of nurses in the community, it's just going to make cost per visit go up in that nursing discipline. So, we're cautiously optimistic, we feel good about the changes that we've made, but we also recognize the global pressure that we're seeing in the nursing discipline.

And then, finally, as it relates to volumes, if you look at the data in the slide deck we've provided, yeah, I think we've made nice progress this year incrementing our visits per episode down over the course of the year from the second quarter being a bit of an anomaly, but over the course of the year [ph] we've seen some (00:30:10) improvements there, but I think there is room we really didn't get Metalogix carefully deployed until mid-year, and given that the focus obviously this year has been so much on staffing and managing COVID-related risk, I would say it wasn't as successful an implementation as we had anticipated. It didn't come out of the gates as fast as we would have anticipated because there were so many other distractions. And so certainly, we see some opportunities going into 2021 further leverage the effectiveness with which we're using those tools. And so, yes, we're encouraged about the trajectory and the momentum that we take into 2021, but I think we're also cautiously optimistic because we recognize that the COVID risk is not behind us, we can't fully predict what's going to happen here in the first half of the year relative to COVID impacts on volumes, and we're not quite sure about those nursing costs. And so, we're going to keep pressing forward, we're encouraged by the margins we've been able to produce and we're going to work hard to sustain those, but I think we're keeping a cautiously optimistic tone in our projections.

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<Q – Whit Mayo – UBS Securities LLC>: Can we – is there any way maybe to circle a number that you've contemplated within the plan this year for the inflation across your nursing discipline, maybe what it costs per visit, anything directionally that can kind of give us a marker to look for going forward?

<A – April Anthony – Encompass Health Corp.>: Well, not specifically there, but obviously if you look at the 2% to 3% wage increases that were reflected in our guidance, we think those will be disproportionately allocated to the nursing discipline. You may see a lesser rate in some of the therapy disciplines where supply and demand imbalance is not the same, higher proportion of those wage increases across the board [indiscernible] (00:31:54).

<Q – Whit Mayo – UBS Securities LLC>: Okay. Thanks.

Operator: Your next question comes from the line of Brian Tanquilut of Jefferies.

<Q – Brian Tanquilut – Jefferies LLC>: Hey. Good morning, guys.

<A – Mark Tarr – Encompass Health Corp.>: Hi, Brian.

<A – Doug Coltharp – Encompass Health Corp.>: Good morning.

<Q – Brian Tanquilut – Jefferies LLC>: So, I guess, Doug, my question for you, as we look at where your guidance is and I'm sure you've looked at where Street numbers are, I mean, how are you thinking about what the delta is there? What do you think the Street missed, and just any color that you can give in terms of the moving parts and the guidance that investors might have missed in driving some of that disappointment today?

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. So, most of the models aren't detailed enough. The analyst models aren't detailed enough for me to be able to point to the specific areas of differential. I will say that our guidance is driven off of our budget, and our budgets are built in a painstaking brick-by-brick fashion from the bottoms-up. So, suffice to say there's substantial more detail that goes into the provision of our guidance. Having said that, some of the areas that I may think that I think the analyst may not have had complete visibility into relate to things like the $15 million to $20 million in preopening and ramp-up cost associated with our new hospital activity, the normalization of some of our employee benefits, particularly group medical expenses in the IRF side of the business, and just I think some of our expectations regarding the impact of COVID on both volumes and expenses in the first half of the year. Those would be the areas I would point to as the primary differences.

<Q – Brian Tanquilut – Jefferies LLC>: Got you. And then, Mark, I guess you tweaked the long-term guidance ranges, and so, how're you thinking about whether it's the progression back to the sort of the endpoint goal for 2025 in terms of revenues or earnings or is that an indication of your belief in the fundamentals of the business? And then what kind of recovery pace are you thinking about to get to these revised long-term growth targets?

<A – Mark Tarr – Encompass Health Corp.>: Yeah. Brian, I think our growth targets reflect our confidence in the long-term opportunity to continue to grow our business, the demand for our services. I mean, we've come out this year, and we're experiencing now the typical seasonal rebound that we would have seen in the past in both our operating segments. There're challenges in terms of meeting all that demand right now given the numbers of quarantined staff and the capacity caps that Doug mentioned in terms of having semi-private beds more hospitals, but we're very bullish on the opportunities for us. We've got the very robust pipeline. We've got 8 hospitals coming on this year, 10 already announced for next year. We'll continue to look for opportunities for acquisitions in home health and hospice. So, the fundamentals are there to provide these growth targets that we have in our longer-term outline here.

<A – Doug Coltharp – Encompass Health Corp.>: And Brian, if I can just add to that what we've done is essentially set – reset the CAGRs off of a lower 2020 base to arrive at the same station in 2025 that were implied with the growth targets that we laid out at our Investor Day last March. And that's reflective of the fact that our shortfall for 2020 that resulted in the lower base is solely related to COVID, and that we believe – we believe that the impact from COVID is temporary and doesn't reflect any fundamental change in the underlying business demand for either one of our two business segments. And that on top of that, our growth plans have not changed. We continue to invest, as Mark just said, heavily in capacity additions in the IRF space and we'll continue to be in acquisition mode for home health and hospice as well as pursuing the attractive organic growth opportunities that exist within that business segment.

<A – Mark Tarr – Encompass Health Corp.>: Brian, any answer that we have right now is just near term, and it's all tied to COVID and how quickly we'll be able to respond with vaccines and get on the other side of this pandemic.

<Q – Brian Tanquilut – Jefferies LLC>: Awesome. Thanks, Doug.

Operator: Your next question comes from the line of A.J. Rice of Credit Suisse.

<A – Mark Tarr – Encompass Health Corp.>: Good morning, A.J.

<A – Doug Coltharp – Encompass Health Corp.>: Good morning, A.J.

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Hey, everybody. Maybe just a follow-up on that previous discussion around the long-term targets, I appreciate you guys reinstating that. I think though if you string out the midpoint out to 2025, you end up with an EBITDA target that's about, or at least we do, maybe I'm calculating wrong, about $70 million below the midpoint of the March 2020 Investor Day outlook, and the margin is about 90 basis points' lower, and about 18.5%. Is there something that's changed in there because it sounded like from your previous comment just a minute ago though you thought it was sort of coming out at the same point. But that's not actually what we get. And I wonder how you're factoring in this demonstration project that CMS has put forward, do you think that's going to have any impact on the outlook if that goes into place next year, any thoughts on that?

<A – Doug Coltharp – Encompass Health Corp.>: So, A.J., I'm actually getting midpoints when I compare the two that are substantially closer than the delta that you just suggested. I'm not going to say that's exactly the same number, but they're closer, so I don't want to get into a math reconciliation exercise...

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Right.

<A – Doug Coltharp – Encompass Health Corp.>: ...here.

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Okay.

<A – Doug Coltharp – Encompass Health Corp.>: With regard to review choice demonstration, there's more that is unknown about that than there is that is known about that. It's really in the very early stages. It could very well have a positive impact, and then it's going to reduce the amount of claims denials after the fact. What we've already demonstrated in our home health business is that because we are very process-oriented throughout our company to begin with and because we have great management information systems in place, we can adjust as well to new regulatory and/or process requirements as anybody that is out there. And I'm confident that if we move forward with review choice demonstration in the IRF business, we will execute, do it effectively, and it will not be disruptive to our business.

<A – Mark Tarr – Encompass Health Corp.>: A.J., as Doug noted, but it certainly further substantiates the investments that we made in our electronic medical record a number of years ago so that we see this is positioning ourselves to our documentation and the standardization across the board to make sure that the documentation is there and thrilled to put us in a real good position if RCD were to be moved forward.

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Okay. All right. Thanks a lot.

Operator: Your next question comes from the line of Matt Larew of William Blair.

<A – Mark Tarr – Encompass Health Corp.>: Good morning, Matt.

<A – Doug Coltharp – Encompass Health Corp.>: Good morning, Matt.

<Q – Matt Larew – William Blair & Co. LLC>: Hi. Good morning, guys. Doug, I want to follow up on Brian's question, but let's just maybe remove Street models from the discussion and instead focus on the second half of 2020 versus 2021. So, I think even after adding back or excuse me removing those start-up costs that you alluded to, the EBITDA margin applied for 2021 are about 100 basis points lower than second half of 2020. And obviously you've characterized today a number of tailwinds on the home health side, returning volumes on the IRF side. And I think sequestration, but that's coming back into the picture that wasn't expected for the first quarter, certainly, that was an extension. So, I guess, I'm just trying to think what are the other things that we might have to take, is it acuity reversal, COVID costs or maybe bad debt increases, PPE, are there any numbers you can maybe generally point us in the direction of that would help kind of bridge that gap?

<A – Doug Coltharp – Encompass Health Corp.>: So, Matt, tell me again, you're trying to reconcile the second half of 2020 to the second half of 2019?

<Q – Matt Larew – William Blair & Co. LLC>: No, sorry. Second half of 2020 relative to what the EBITDA margins for 2021 are, right.

<A – Doug Coltharp – Encompass Health Corp.>: Right.

<Q – Matt Larew – William Blair & Co. LLC>: And so, the second half of 2020, EBITDA margins were about 19.7%, and I think the guide for 2021 is 18.5%, and I'm just trying to reconcile that given the positive momentum you talked about.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. And you moved past the sequestration expenses pretty quickly, but I think that that's at least half if not more than half of it. And then, I think if you combine that with the likely timing of a lot of the preopen and ramp-up costs for the hospitals that you've substantially closed the gap just between those two numbers.

<Q – Matt Larew – William Blair & Co. LLC>: Okay. Will look again. I thought I already contemplated that in my model, but fair enough. Maybe I'll just ask then about the Medicare Advantage side. You've given some nice updates throughout the year about pricing your volume trends, would be curious there, and then any additional color you can give on the United contract you alluded to. Is it a preferred provider relationship to an extent? Is there risk-sharing involved, that'll be great.

<A – Mark Tarr – Encompass Health Corp.>: I'll ask April to cover the United contract first.

<A – April Anthony – Encompass Health Corp.>: Yeah. So, we're excited about joining the panel of national contract providers for the UnitedHealthcare contract, but it's a little bit of a good guy, bad

guy combination on that. I think in the long run, being part of that national contract is going to give us volume opportunities. It's going to give us better opportunities to serve patients coming out of our IRFs. But historically, we have gotten some United business in more of a one-off fashion and we've been paid episodically for that business. And so, when we shift to this national contract, as much as we're excited about it and excited that it has a value-based element of bonus based on quality performance, we also recognize that there could be some near-term margin pressure brought on by the shift from the episodic payments we had in 2020 and prior to beginning in February 2021, more of a fee-for-service payment with an after-the-fact bonus kicker. So, we think it's a good relationship. We think it'll bring over time as we get all of our staff off of quarantine, we think it brings the ability to grow that relationship pretty significantly, but we also recognize that in the near term, it'll put a little bit of margin pressure on us in the early parts of 2021 as we kind of re-baseline that contract.

<A – Mark Tarr – Encompass Health Corp.>: Matt, I'll ask Barb Jacobsmeyer to give her insights on what we're seeing from MA plans with regard to our hospitals.

<A – Barb Jacobsmeyer – Encompass Health Corp.>: Yeah. So, as you've seen, we have nice growth. Obviously, the relaxation between May and September of the pre-ops assisted in 2020, but as you know, we already had seen some nice growth in MA back in 2019 that continued in 2020, and we'll continue to be focused on that in 2021. I think the great thing for us is that we saw admissions to IRF here in 2020 that maybe in the past they would not have sent to us. Some of that was due to the waivers, some was because SNFs were really unable to accept patients maybe due to COVID outbreaks or other limitations in the SNF. So, we now have more data on the outcomes of those patients. And that's going to assist us as we continue our discussions, particularly with the medical directors of these MA plans so that we can really talk about the value proposition directly as it related to their patients.

<Q – Matt Larew – William Blair & Co. LLC>: Okay. Thank you.

Operator: Your next question comes from the line of Kevin Fischbeck of Bank of America.

<A – Mark Tarr – Encompass Health Corp.>: Good morning, Kevin.

<Q – Joanna Gajuk – BofA Securities, Inc.>: Good morning. Actually this is Joanna Gajuk filling in for Kevin. Thanks so much for taking the questions. But just I guess a follow-up on the discussion around the long-term growth targets. So, I guess you were saying that the numbers are a little bit closer, but would you describe it as kind of those targets implying higher revenue, but maybe slightly lower EBITDA because I guess that's what we are also getting at when we do our math. And then, I guess if that's the case is there any particular area where you would point to in terms of the lower margins either segment-related or something around PPE cost or was there anything in terms of these long-term growth targets?

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. I think you're all reading a degree of precision into the five-year CAGR that simply doesn't exist. These CAGRs reflect the fact that the base for 2020 is lower than we had anticipated last March. And the delta between those we attribute 100% to COVID, which we ascribe as a temporary impact that we anticipate will fully dissipate through the course of 2021. So, in addition to the lower 2020 base, you have some residual impact in the first year of the transition. Beyond that, you've got 200 basis points spread on five-year CAGRs, so allow for some rounding.

<Q – Joanna Gajuk – BofA Securities, Inc.>: Okay.

<A – Doug Coltharp – Encompass Health Corp.>: I think what you'll see is the base is lower, we've already talked about that. Our growth plans on top of that have not changed, and you see that reflected in some of the assumptions that we put out there. So, we're going to arrive at

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essentially the same station in 2025. If the margin is 10 or 15 basis points lower or higher, so be it, there are multiple ways that we can get from here to there, but the targets that we're shooting for in 2025 are essentially unchanged from those that we discussed with you in March of last year.

<Q – Joanna Gajuk – BofA Securities, Inc.>: Okay. Great. That's what I was just trying to confirm based on how you responded to the question. So, thank you for that. And if I may just I guess partially follow-up on some things you mentioned in your introductory remarks around SNF-at home. I guess the association is relatively optimistic that something could be actually or registration could be introduced to Congress, obviously we don't know when it would be passed or is not. But can you just talk about I guess this is question is for April, how Encompass could participate in an extended benefit as such, SNF-at-home. I guess you mentioned about contracting with personal care providers, so would that be enough, would you be able to cover all your markets with that because I guess you do not have actual presence in terms of personal care services. So, could you just frame for us how you think about this opportunity before Encompass? Thank you.

<A – April Anthony – Encompass Health Corp.>: Yes. So, happy to share about that. So, as you know, we don't have the personal care division as part of our organization. And that was why it was critical for us to be able to create some key partnerships with private duty focused companies that had national presence so that we could ensure that we could respond in the same timely fashion that some of our competitors who have that service line are responding. And so, we feel like we've got those relationships in place, and are beginning even to kind of leverage those when we have family structures that can support that private duty service line. As you know, we are hopeful that there will be a version of SNF-at-home that actually makes it into legislation, and then they become the payer source for those private duty services acknowledging that we can likely provide that care to a certain cohort of patients at home, less expensively than they would be cared for in a SNF facility. But it'll take more than the average $50-ish we get today out of Medicare to do that.

So, we think that there is certainly legs to that program, and that if it did find a funding source that we can care for those patients effectively, that we've got both the technology tools to be able to support virtual care, supplant that with our contractual relationships from private duty, and then really use our historically-strong quality and clinical performance on the skills side to keep those patients safe at home at a lower cost. So, we look forward to that program evolving, and are looking for new ways that we can execute and deploy on it before there is even a alleged piece of legislation that might fund it in certain instances.

<Q – Joanna Gajuk – BofA Securities, Inc.>: Yeah. Thank you.

Operator: Our next question comes from the line of Frank Morgan of RBC Capital Markets.

<A – Mark Tarr – Encompass Health Corp.>: Hello, Frank.

<A – Doug Coltharp – Encompass Health Corp.>: Good morning, Frank.

<Q – Frank Morgan – RBC Capital Markets LLC>: Good morning. I hopped on late, so I apologize. And I think April was just at the point of making some comment about volumes in December. So, I guess, I'll ask, did I understand that correctly? And then do you have any commentary around what you're seeing so far in the first quarter both in the home health care side and in the IRF side. And I apologize if you've talked about it before I hopped on.

<A – Mark Tarr – Encompass Health Corp.>: Frank, I'll talk about – this is Mark. I'll just cover where we are at least up to this point. As you know, we typically have a seasonal rebound after the holidays. And we've seen that. There's a strong demand for our services in both of our operating segments which is a testament to the confidence that we have going forward. We are challenged in certain markets with staff that are quarantined. The positive news on that is both segments have seen a decrease in the number of quarantined staff over the last week and a half-or-so. So, that is

at least trending in a more positive manner. When we get more staff back, we'll have fewer markets that we have been capped on volume because of staffing restrictions. And then, we also have certain marketplaces where the hospitals have a higher number of semi-private rooms where we've had to enforce isolation requirements that have temporarily capped us off in those hospitals, but demand is very strong and supports our thoughts that any uncertainty that we have is near-term uncertainty all tied to COVID, and the opportunities that we have getting on the other side of this pandemic.

<Q – Frank Morgan – RBC Capital Markets LLC>: Got you. And where are you in terms of total amount of your staff that has been vaccinated now for COVID?

<A – Mark Tarr – Encompass Health Corp.>: So, Frank, we have a total of about 6,800 employees that have been vaccinated with a small portion of those, they had their second doses. So, we're getting out to the marketplaces, we've had I think close to 70% of our total staff respond that they would like to have the vaccine. So, we'll continue with that distribution process. As you know, a lot of volatility from state to state in terms of the effectiveness of giving it out to the marketplaces, but we continue to see progress with that.

<Q – Frank Morgan – RBC Capital Markets LLC>: Got you. And then, just last one, I know that April made the comment about the nursing shortage, but I'm just curious where some of the pressure because of shortages, was that limited and maybe back to the question what about on the IRF side, are you seeing something similar, and is that driven more by people being – actually having COVID and can't go into the home and aren't they available in the work pool or is there anything else that's driving that?

<A – Mark Tarr – Encompass Health Corp.>: Frank, I'll ask Barb Jacobsmeyer to weigh in on what we're seeing on the IRF side?

<A – Barb Jacobsmeyer – Encompass Health Corp.>: Yeah. On the IRF side, it's been really more about the folks being out in quarantine, and so again as Mark mentioned, we anticipate that all those folks coming back. I would say that we did see early on some of our more experienced older nurses decide that maybe they just didn't want to be in the workforce at this point because of some fear and some anxiety. The good news is though as we're hearing back from some of those saying that now that the vaccine is out, they want to come back, they want to be able get the vaccine and get back to work. So, I think that we will see more of that as we get more of the vaccines.

<A – Mark Tarr – Encompass Health Corp.>: Frank, I think just overall nursing in general, and all the clinicians who're treating these COVID patients, until there was a vaccine that was being rolled out, there really – there was no end at the light of the tunnel. So, they didn't know when we were going to get on the other side of this pandemic, and really caused a lot of stress from the workforce and that is not specific to our clinicians, but the industry as a whole. So, I think the vaccine has brought some hope and some sense of an endpoint to look forward to – for clinicians.

Operator: Your next question comes from the line of Andrew Mok of Barclays.

<A – Mark Tarr – Encompass Health Corp.>: Good morning, Andrew.

<Q – Andrew Mok – Barclays Capital, Inc.>: Hi. Good morning. I wanted to follow up on the home health volumes. Your same-store home health admissions remained moderately depressed due to the continued drag from assisted independent living facilities and lower elective procedures. Can you comment on how admissions trended in the rest of the portfolio? And do you see a path back to mid-single-digit organic volume growth in 2021 even with some of the lingering COVID headwinds? Thanks.

<A – April Anthony – Encompass Health Corp.>: Yeah. Thanks. Thank you for that question. So, we did see a meaningful decline from the three areas that we called out: the admissions of patients that are discharging from SNF, the elective surgeries and senior living communities, combined roughly about 3,800 admission decline came from those sources. As you saw, our overall organic growth was down about 2%. So, if you add those 3,800 back in there, we really had a strong performance in the other sectors to make up that difference. I think had it not been for that 3,800 decline, you'd be at about a 7% increase. Now, I realize I'm making a lot of assumptions and projections about what could have been, but I think that when you look specifically at the cause of those, we do feel very encouraged that getting back to a strong organic growth posture as we see this virus subside in the second half of the year is something that we believe is very possible, and we think that we replace the lost referrals and lost admissions with new sources that are sustainable. And so, I actually think we can come out on the other side of this recovering what we used to have and maintaining what we have developed and come out with really a win-win combination once we get past the COVID period.

<Q – Andrew Mok – Barclays Capital, Inc.>: Great. Thanks. And secondly, looking at the 2021 EBITDA and EPS guidance compared to the initial 2020 guidance. EBITDA is about 1% lower and EPS is about 5% lower. Can you walk us through some of the assumptions below the EBITDA line that are driving the spread on EBITDA and EPS growth? Thanks.

<A – Doug Coltharp – Encompass Health Corp.>: I think the single biggest line is interest expense.

<Q – Andrew Mok – Barclays Capital, Inc.>: Got it. So, that's driving the entire delta?

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. And I mean, I don't have that right in front of me but I believe that's the primary driver.

<Q – Andrew Mok – Barclays Capital, Inc.>: Okay. Great. Thanks.

Operator: Your next question comes from the line of Pito Chickering of Deutsche Bank.

<A – Mark Tarr – Encompass Health Corp.>: Good morning, Pito.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Hey. Good morning, guys. Thanks for fitting me in. Two quick questions for April. When I look at the payer mix in 2020 and where've you taken the cost per visit in the fourth quarter, and all the data that you collected, how should we think about the new cost structure and leverage from analytics converting into you guys getting more aggressive with MA and commercial contracts? And I guess it definitely is this new contract with like in the United the tip of an iceberg if you guys are signing the contracts?

<A – April Anthony – Encompass Health Corp.>: Yeah. I certainly think that we have a lot of momentum moving in that direction. And we've always been very discerning about the relationships that we wanted to enter into. We wanted to focus on those that we felt very comfortable that the reimbursement level supported the level of quality care that we wanted to deliver. And so, we've historically lagged the industry in non-Medicare relationships because of that. And I think that's beginning to change as we continue to get more and more efficient in our operating model lowering our cost base that creates opportunity, but we're also seeing those payers move in the right direction as well and create contracts that not only have higher reimbursement associated with them but also more efficiency relative to their authorization requirements or better said lack of requirement. We're really being very discerning about the contracts that we take. And if there's a preauthorization requirement that's going to become burdensome in time and effort, we're saying no to those.

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And so, I think we're looking for those right relationships where we can be paid well, where we can be a trusted partner who doesn't have to be nickeled and dimed on every visit allocation, but rather is trusted to deliver clinical outcomes, and then in turn be rewarded for those outcomes. Those are the kind of partnerships that we're looking to form. And I think when you get down to – you can look at star ratings. But when we talk to payers, they frankly don't ask us very much or talk very much about star rating. What they instead want to know about is emergent care and hospitalizations. If you look at our statistics in both of those categories, we performed very, very well, and as a result become a very trusted partner to those sources, and a partner that they'll negotiate with for a little better rate. So, I think as the tide continues to move in that direction, you'll see us expanding on those relationships in ways that continue to support our quality care delivery.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Okay. Great. And then a follow-up question for you April again on home nursing. There's obviously huge demand for any employees or nurses who're helping patients in the home setting today. How should we think about wage inflation ahead of normal levels within home nursing during the next year or two? Thanks so much.

<A – April Anthony – Encompass Health Corp.>: I don't necessarily think that home-based care will have a higher inflation rate than other healthcare sectors. I just think that we've seen, as Barb mentioned, we've seen a lot of our older nurses, which tend to gravitate toward homecare for a variety of reasons leave the market early because of COVID. And then, we've seen a lot of our younger nurses who're raising young families leave the market because of some of the childcare challenges that have existed during the COVID period. Hopefully, as COVID subsides, we'll keep both of those cohorts potentially come back to the market, but in the meantime we just see a recognition that hospitals are driving the costs up, and then as a provider in the same market even though we're providing a different type of service, we're having to chase some of those acute care hospitals in what they're having to do to recruit nurses to work their floors. And so, I think it's just something that we're going to be sort of a byproduct, not the leader of the inflationary market, but we're just going to chase the acute care hospital behavior because that's our competitor for the workforce.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Great. Thanks so much.

Operator: [Operator Instructions] Your next question comes from the line of Scott Fidel of Stephens Inc.

<A – Mark Tarr – Encompass Health Corp.>: Hello, Scott.

<Q – Scott Fidel – Stephens, Inc.>: Hi. Thanks. Good morning. I had to hop on late due to another earnings conference call. So, hopefully, this has been asked, but had two questions for you. The first is just if you could give us sort of an initial framework and thinking about the home health and hospice M&A target that that you've included the $50 million to $100 million. Just in terms of sort of bias in terms of home health relative to the hospice markets, and sort of pipeline in those, and then also just obviously not expecting you to comment on the strategic review, but I we're just interested in as we're late to that specific M&A target that you have for the business, whether the strategic review would influence that in terms of the pacing of how we should think it you executing on the M&A plan for 2021?

<A – Mark Tarr – Encompass Health Corp.>: Yes. Scott, this is Mark. So, as you noted, we can't comment right now on strategic review and in a set timetable for that, but the process is ongoing, but I will ask able to weigh in on her thoughts on the acquisition?

<A – April Anthony – Encompass Health Corp.>: Yes. We definitely saw a resurgence in acquisition activity in the back half of last year and things that are kind of a lull that we've experienced at the beginning of the year from both COVID and PDGM transitions is in the rearview mirror now. So, we're seeing a lot of activity in the M&A pipeline, and encouraged that we're going

to be able to find some good options. When we focus on really where will the deployment of that acquisition capital go, we really continue to focus on our consistent three strategies: job number one is that we want to create more overlap markets with our ERPs because we see strong results in clinical collaboration; job number two is we like to build scale and density in markets because we see that having margin improvement opportunity; And then job number 3 is we like to also create that overlap between home health and hospice just like we're doing with home health and IRFs.

And so realistically, if it hits one of those three core criterias for acquisition, we're not particularly focused on home health or hospice more so one than – the one over the other, we really are looking at those three categories and saying which one does this serve best and where can we get those dollars deployed. Multiples are rising obviously, particularly in the hospice sector. And so, we continue to be a discerning buyer. We want to grow, but we also want to deploy our capital carefully and in the way that it can create the best yield for the organization. And so, we're looking at an array of transactions that fit in that three-pronged criteria.

<Q – Scott Fidel – Stephens, Inc.>: Got it. And then just for my follow-up question, just interested in an update on the clinicians' competition model changes that you had implemented. It does seem like that was changes that for the margin profile for home health and hospice in the back half? And just interested in the ability that you have to flex that in 2021 just based on how admissions and volumes for the business end up sort of playing out here if they remain depressed because of COVID, did that model sort of stay in place but if you do see volume start to accelerate, how would you adopt the model to ensure that you have adequate staffing? Thanks.

<A – April Anthony – Encompass Health Corp.>: Yeah. The good news is I think the model flexes itself because what we've really done is sort of lower the base pay and in turn create an incentive in bonus compensation that if you'll work over this lower threshold that aligns with the lower base pay that you can earn back to at or above your compensation level. So, it's really been a win-win, and that it's basically shifted the opportunity for excess productivity to the employee side of the equation. And really as a result, people are really pushing and driving to get to the high-end of what our previous 100% plan was because they've got motivation to get there. But I think we have the natural flex capacity. We didn't lower our number of head count in therapy at all by making this change. As a matter of fact that was the beauty of it is that we could keep our full staff, but really drive efficiency and our productivity realization. So, I think we've got the capacity to grow in that service line – in that discipline as we move into 2021.

<Q – Scott Fidel – Stephens, Inc.>: Okay. Thank you.

Operator: Thank you. I'll now return the call to Crissy Carlisle for closing comments.

Crissy Buchanan Carlisle, Chief Investor Relations Officer, Encompass Health Corp.

If anyone has additional questions, please call me at 205-970-5860. Thank you again for joining today's call.

Operator: Thank you for participating in Encompass Health's fourth quarter 2020 earnings conference call. You may now disconnect.

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