PARTICIPANTS

Corporate Participants

Mark J. Tarr – President, Chief Executive Officer & Director, Encompass Health Corp.
Douglas E. Coltharp – Chief Financial Officer & Executive Vice President, Encompass Health Corp.
Barbara A. Jacobsmeyer – Executive Vice President & President-Inpatient Hospitals, Encompass Health Corp.

Other Participants

Matt Larew – Analyst, William Blair & Co. LLC

MANAGEMENT DISCUSSION SECTION

Matt Larew, Analyst, William Blair & Co. LLC

Okay. Well, good afternoon, everyone. Thanks for sticking with us today here on the second day on, I believe, our 41st Annual Growth Stock Conference in the second, and hopefully last, virtual style. My name is Matt Larew. I cover healthcare delivery and services here at William Blair. I'm here today with members of the Encompass Health management team including Mark Tarr, the CEO; Douglas Coltharp, CFO; Barb Jacobsmeyer, who run the Inpatient Rehab business; and Crissy Carlisle from Investment – Investor Relations. So, thank you to all of you for being with us today.

Encompass Health, as many of you know, is one of the leading integrated post-acute care companies in the country [indiscernible] (00:45) a leading inpatient rehab portfolio, and a complementary home health and hospice business. Before we jump into questions, I just want to point out the compliance note, is that for a complete list of disclosures, you can visit our website, which is williamblair.com.

So, to start, well, we don't have a deck to walk through today. But given then this is a generalist growth stock conference, I do think there's some value in just providing a brief overview of the company. Maybe if you could give us a quick take on history of the company, the market you participate in, and how both those markets and how you've participated in them has evolved over time.

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QUESTION AND ANSWER SECTION

<A – Mark Tarr – Encompass Health Corp.>: Sure. Well, Matt, first, let me say, we're delighted to be here with you today. And for those of you that aren't familiar with the Encompass Health story, I'm going to give you some of the highlights.

As Matt said, we're a national leader in post-acute care. We provide that care in both a facility-based setting and a home-based setting. We have a – from a geographic standpoint, we have a national footprint that includes 39 states and Puerto Rico. So, we had a good coverage there. We operate the company in two operating segments. The first segment being the inpatient rehabilitation facilities or IRFs, you may see the – for short. We have – the IRF segment accounts for about 77% of our consolidated revenues. That segment is made up of 139 rehabilitation hospitals, of which 52 of those are joint ventures with acute care hospital systems, and that's been a good business model for us that we've had now in place for over 30 years in terms of our – when our first joint venture facility was established.

At that scale, it makes us the nation's largest owner operator in terms of the patients treated, revenues, and number of freestanding hospitals. We're asked quite often in terms of what that means in terms of market share. About 30% of the Medicare patients receiving IRF level care this year will receive those in an Encompass Health facility, so we're quite proud of that.

If you think about the types of patients that we treat or the diagnostic categories, just to name a few, stroke and neuro makes up about 40% of our total discharges. Other common diagnostic categories would be hip fractures or other orthopedic complications. And then those hospitals that we have that have an affiliation with a trauma center also have a fair number of brain injuries and spinal cord injuries. So, we are proud of the fact that we can handle a high-acuity patient. We're also proud of the fact that we have really set ourselves apart with our expertise, particularly among the stroke and neurological patients.

In terms of just our hospitals, for those of you that aren't familiar with what a rehab hospital is, it's licensed as an acute care hospital. It's a specialty track within that licensure. We don't have ERs. We don't have operating rooms. But nonetheless, if you walk through our hospital, it would look very similar to what you would see in just the journal medicine for – in an acute care hospital, med-surg. We're required to provide 24/7 nursing coverage. In terms of other staffing expertise, we have a podiatrist and a full complement of attending and consulting physicians. We also have physical therapists, occupational therapists, speech therapists and some hospitals have respiratory therapists that provide the care. And we do a minimum of three hours a day of therapy in our hospital. So, it's a fairly intensive program that we provide.

On the second segment, which make up the home health and hospice, which is the balance of our revenues or 23% of our consolidated revenues. That is split up between 80% of that is home health and 20% is hospice. With that [indiscernible] (05:22) makes us the fourth largest provider of Medicare-certified home health services with 241 locations. I guess that it's actually 250 now since we announced the Frontier acquisition of this week. And then in terms of services provided, there'd be skilled nursing. We also have a full complement of therapeutic services relative to physical therapy, occupational therapy, as well as a speech.

So, that's kind of overview of the two operating segments. We see our competitive strengths that differentiates us from the other providers in the space. One is our clinical outcomes. In both segments, we exceed the national averages and the national databases that are kept on each. We're the most cost effective provider in both segments in terms of just managing our cost effectiveness. We have extensive use of technology. Well, that's our clinical information system and our rehab hospitals that we have begun to extract data from, that helps us with our predictive modeling and other analytic opportunities or the home care or home-based which is the

predominant system used in the home health industry. Like to see ourselves as being the super users.

And then we have very strong financial position, a very strong balance sheet, that we also think provides us with a competitive advantage. All the strategy that we have around the growth has underlying fact with a strong demographic tailwind. Our average age patient in our hospital is 76, 77 on home health. If you look at the growth rate of that particular age cohort, you see that's about a 5% CAGR. It's just a – it's matter of fact as we all get – as we all age and get older, the likelihood of the fact that we'll need some type of inpatient rehabilitation is greater.

So, that continues to drive the demand for our services. And it's also at a time where you had this increasing demand, but very flat capacity. There's not been a lot of people that have been adding beds or capacity in the IRF sector. So, that also helps drive the rationale for our de novo growth that you see and we'd like to talk about. If you think about just our longer-term growth targets, which we put from 2020, 2025, it's 8% to 10% CAGR for net operating revenues and adjusted EBITDA, and then 5% to 7% CAGR for adjusted free cash flow. So, that is a mouthful in a short period of time, but hopefully that gives your listeners a bit of an overview of the two segments that we operate in.

<Q – Matt Larew – William Blair & Co. LLC>: That's a helpful setup to the rest of the discussion. In the first place, I'd like to go to that discussion as asking a few questions around COVID. And so the first quarter results and some of our survey work we've done suggests that, I think, volumes at large seem to be largely back to pre-COVID levels. But there's quite a variety in there, depending on the specific service line, not just with Encompass but within the industry.

So, we've seen those trends continue to improve throughout May. So, would just be curious if that's consistent with what you're seeing and maybe the areas of your business that have been particularly strong returning and others that you're still waiting to come back to where they were pre-COVID.

<A – Mark Tarr – Encompass Health Corp.>: Yeah. So, the end of the first quarter and then the K that we subsequently filed, we've seen the population as a whole start to gain confidence in seeking healthcare. And I attribute that to the increased vaccination rates. We've seen it in our business in terms of the number of COVID patients that we're treating has drastically declined. That has helped us as we looked at the impacts.

For instance, when we were in the peak of the pandemic, we had as many as 30 hospitals that had some sort of cap on volume because of the rooms that we had have isolated patients in that limited our capacity. We had hospitals that had a number – a substantial number of staff out on quarantine to where we had to cap the volume because we didn't have the staff to treat them.

Both of those factors have declined now to an immaterial number. Just last week, we had, I think, two hospitals that had some sort of capping due to staffing. So, we've seen a diminished impact from COVID, which has also, from an external standpoint, we've seen the number of elective procedures increased in each successive month throughout the year. We have seen the number of elective referrals, particularly to our home health, has continued to increase. We've seen it in our hospitals as well. And we've been quick to say that a 76 or 77-year-old is probably not going to be the first to seek out elective procedures. But we do think that we're starting to see them enter that fold as well.

So, all of those are contributing factors to starting to see our volume levels get back, if not ahead of where we were pre-pandemic. Some of the trends in terms of the types of patients were being referred from acute care hospitals are reaching back to some – at normal pattern. And we're very glad to see things are starting to get back to maybe 2019 or certainly before the pandemic impacts that we saw last year.

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<Q – Matt Larew – William Blair & Co. LLC>: That's great. And so, Mark, you referenced there some of the turmoil that you and others in the industry have had to deal with over the last year-plus. But COVID has also led to some meaningful opportunities for companies that were able to act quickly in order to make change in end market demand. So, just curious if there are things you could point to in terms of changes in end market dynamics, customer behaviors or preferences, or perhaps your relationships with customers, or your own competitive position and capabilities that – emerging from COVID, you think would be helpful to the company long-term.

<A – Mark Tarr – Encompass Health Corp.>: Yes. So, I'm very proud of the way the company handled itself during the midst of the pandemic. And by that, I mean that we came out early on. Once we had determined that we could effectively treat COVID patients, we were there for all sources. And we were taking COVID patients and showed the willingness and the capability of treating COVID patients early on when others in post-acute sector either wouldn't accept COVID patients or showed the inability to effectively treat those COVID patients.

And so I think we continue to establish our profile of having ability of treating a high-acuity level patient. We continue to establish our goodwill with the referring acute care hospital systems, whether they were our partner in a formal manner or an informal manner. We were there to be part of the answer and part of the solution as part of the pandemic. And I think that has definitely continued to show as we have worked our way out of the pandemic in terms of longstanding referral relationships with acute care hospital systems. And it also gave us the chance to show the MA plans what we could do with rehabilitation patients, and gave us a chance to get exposure to some payers from a value proposition standpoint that maybe we did not have a chance in the past, but gives us a chance to have relationships going forward and continuing to show what we can do for our quality outcomes.

<Q – Matt Larew – William Blair & Co. LLC>: And so, thinking about just the back half of 2021 here. As vaccination deployment continues, we've seen CDC recently changed guidelines around requirements for vaccinated individuals. What do you see as the biggest growth drivers for the back half of 2021? I note on the first call, you mentioned the restriction of facility access for things like SNFs [indiscernible] (14:28). And, of course, partly just a little bit due to elective procedures. So, there's certainly a lot going on in the end markets. But just curious, if I think about the back half of the year specifically, what items are you're targeting at all for key growth drivers?

<A – Mark Tarr – Encompass Health Corp.>: Yeah. So, the back half – we factored in for this back half the year within our guidance that there would not be longstanding impacts from COVID, that things would be back to normal. So, it is things such as elective procedures coming back. The fact that we have as many as 15% of our admissions into our home health come from assisted living facilities or nursing facilities. We would expect to see those come back. We now have access to those settings, but the volume within those settings [indiscernible] (15:17) has not recovered back to its full point and historical highs. We think it will, and we fully contemplate that we will be there and help them care for those patients as we've done in the past. But their volumes aren't back yet. But we do think that in the back half of the year, that will continue to normalize out.

We think that you'll just see continued confidence in the public in accessing our healthcare system. I do think that there is reason to believe that there have been deferred health care needs among patients, and that you'll start to see them reach back out to the healthcare system. And we would expect to see some of those normal patterns that we've seen in the past for both our home health and our IRFs.

<Q – Matt Larew – William Blair & Co. LLC>: And then the final one around COVID, Doug, just curious if there are opportunities for Encompass to operate long-term as a more efficient higher-margin business based on efficiencies you've gained during COVID. Maybe this is an opportunity

also to provide a window into some of the cost structure changes you made in response to PDGM, which just coincidentally occurred during COVID.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. I think where the margin opportunities exist, it is on the home health side and really is around both the – predominately in the visits per episode, which is the direct outflow of the deployment of Medalogix and becoming more refined in our care planning on a per patient basis. Even though we had fully deployed that module across our platform by the end of June last year, given some of the limitations on how we operated related to the pandemic, we weren't able to fully utilize it. We're making great strides this year. I think it's showing up in the visits per episode trend. And we think that there's further upside on that.

Cost per visit, we've – I think we've been very good about managing. Is there room to continue to refine that as we push up the percentage of our clinicians that are operating at the top of their license? I think there is some, but we're ahead of the pack there. And those would be the primary drivers of margin on the home health side. For both of our businesses, as we transition into 2022, one of the things we're going to face on the top line is the reinstatement of the Medicare Sequester, and that's going to have the impact of wiping out most of the market basket update we would see for Medicare for 2022 . And when your inputs are continuing to rise at normal levels, that creates some near-term margin pressure. And then compounding that for 2020 on the IRF side is going to be the impact that comes from the opening – pre-opening costs and the ramp-up costs of new hospitals. So, both the 8 coming on in 2022 and then 12 will be opening in 2023.

On that latter point, I would expect that to reverse beginning in the second half of 2023. And there, the EBITDA benefit we'll be getting from the openings in 2021 and 2022 should overcome the incremental pre-opening associated with hospitals beginning in the back half of 2023, and should be a positive move forward. So, some puts and takes on the margin side. It's going to be tough to get margin traction in 2022. Still a little bit of a headwind in 2023. I like the longer-term trend on that as you move from 2023 and beyond.

<Q – Matt Larew – William Blair & Co. LLC>: And [indiscernible] (19:10) I think that sequester reversal is certainly something we have in our models, but – so the investor should be aware of as they're building out expectations for any Medicare operators in 2022.

So, moving now beyond COVID and thinking about M&A, obviously you just closed the Frontier deal. And your targeted $50 million to $100 million [indiscernible] (19:30) M&A per year is kind of the typical number. Just curious what you're seeing in terms of the size and tilt of the pipeline, home health versus hospice. What size the assets the company is looking at? And then, when this consolidation opportunity that was going to be driven by PDGM, when do you think that might really start to come in to view?

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. So, beginning in – we had similar comments we had made previously. Beginning in the second half of last year, we started to see a pickup in M&A activity predominantly in the hospice space, and predominantly around some of the larger properties that were in [indiscernible] (20:07). And you saw some of those trade rather late year and they traded at pretty significant multiples. We had been involved in a number of those processes, and ultimately they got a little too rich for us and we didn't wind up moving forward. I think the reason that last year was focused on the hospice space is that hospice was not subject to a major payment model change as were home health and the IRF business. And that business also was not as directly impacted by COVID. There were some issues around length of stay, but for the most part, volumes remained pretty consistent. And therefore, it was easier for buyer and seller to engage in some reasonable degree of price discovery, at least around a normalized EBITDA.

We saw home health kind of join into the conversation at the beginning of this year, and we feel good about the fact that we're seeing opportunities there that are both large and small. We're one of the few players that can really capitalize on some of the smaller opportunities because of our

strategy of filling in additional markets that overlap between our home health and IRF and also creating density in markets where we have home health or complementing existing home health and hospice assets with the other business line.

There are a number of opportunities that we think will be available that are in the range of Frontier. And if the geography makes sense and if there aren't any quality issues, we'll take a look at those. The competition remains fierce on any assets of size. We got a lot of capital that's available in this market based on the multiples of the publicly-traded peers and based on the support that the PE firms are getting from the leveraged finance markets. And so, we haven't seen anything, but continued pressure on the margins when you're talking about any asset of scale.

<Q – Matt Larew – William Blair & Co. LLC>: Well, obviously, I had this dialed for later in the conversation, but you mentioned nicely-sized assets at the market, valuations of peers, and interest of PE – so I have to ask it now, I guess, which is, I understand you're not going to comment on your strategic review process. I think there's an update coming on the second quarter call. Just wanted to gauge where things stood at with respect to finding a replacement for April on the home health and hospice business with [indiscernible] (22:27) tenure set to conclude in a couple weeks. At least, the way I've been thinking about these two processes is they were inherently aligned even if they were separate just because finding someone to lead this business, I presume, requires an understanding of whether long-term that business is going to sit either within Encompass or elsewhere.

<A – Mark Tarr – Encompass Health Corp.>: So, Matt, as you know, we've said that we've engaged a third-party search firm to do a national search. There has been a significant amount of interest in this sector overall. We do expect, and we're confident, that we'll find a good leader, and look forward once we have found that person and brought them on board. We look forward to making that announcement.

<A – Doug Coltharp – Encompass Health Corp.>: And, Matt, you're absolutely right that having a replacement leader in place is a condition precedent to a number of the alternatives that are under evaluation right now, not for all of them, but for a number of them.

In terms of the overall process, we've been hard at work on the evaluation, the due diligence, and the preparations since we made the announcement in mid-December of last year and feel like we have made very good progress in terms of where we are today.

<A – Mark Tarr – Encompass Health Corp.>: And you're right. We've said it. We fully intend to give an update on our Q2 earnings call.

<Q – Matt Larew – William Blair & Co. LLC>: That was my next one just to confirm that, so that's great. So, you mentioned earlier that Medicare Advantage growth on your side, and I thought that may be an interesting area of test question for Barb, which is that this is – the MA growth really was accelerated pre-COVID, but it's something that was a big growth driver throughout COVID. So, just curious, as you think about MA growth both in the back half of this year and beyond, what patient categories maybe are most interesting for payers, maybe help people understand the nuance of the pre-authorization removal that was in place just so investors can have a sense for what they should expect for MA growth on your side?

<A – Barb Jacobsmeyer – Encompass Health Corp.>: Sure. So, the MA pre-authorization did go away during the peak flare of COVID, around May, June and July. Most of the plans did waive that pre-authorization. What that allowed was that there are groups of patients that historically MA has really strongly pushed toward SNFs. As you know, they've always been a good supporter of sending the stroke patients, and we've grown in that diagnosis over the past two years. But there are groups of patients like other neurological patients, hip fracture patients, that they tended to pretty significantly push toward SNF.

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And for various reasons, obviously during COVID, it became imperative for us to take those patients. One, there were patients' fear about going to the skilled facility during COVID. Another is that the acute care hospitals were very anxious to get the patients that could go to post-acute out as soon as possible so that they could have those beds available for their patients that had COVID. And in many times, whether you had COVID or not, the SNFs do take longer to take the patients out of an acute care hospital. They need them to be more stable. And so, for various reasons, we were able to take more diagnoses from MA than in the past.

What that's allowed us to do now is ever since the authorization went back into effect, we now have data on those MA patients in our hospital and those outcomes to really go and meet with those local and regional MA providers to talk about the success that we had in getting their patients home and then keeping them home. So, that will continue to be a focus for us. And the great news is now, it's not just using Medicare claims data, but data on MA's actual patients that ended up coming to our hospital during that time period.

<Q – Matt Larew – William Blair & Co. LLC>: It strikes me as a sustainable change. Of course, the SNF to home health, perhaps there's more [indiscernible] (26:25) in terms of the discrepancy and preference change, but SNF – or maybe not for all patients, but for a lot of these jump-ball patients, at least the feedback we've gotten and seen the numbers, from company's report, but that seems like a sustainable change. And you guys really have a good case to make for why you deserve more of those patients. You've been hard at work building data around that, I know, for some time.

<A – Barb Jacobsmeyer – Encompass Health Corp.>: Yeah. And like I said, the great part now is that we have the patients that were able to come to us during that wave [ph] were the pre-op (26:53) and can use that information because it really only takes one readmission of those patients back to an acute from a SNF or the SNF to lose what would be their potential value proposition from a cheaper cost setting, if you will. And so I think we have great data to continue our trend there.

<Q – Matt Larew – William Blair & Co. LLC>: That's great. I've wanted to ask a question before we ran out of time here in the next 90 seconds around ESG. And ESG criteria are being incorporated into more investment decision-making processes, and certainly something we are hearing increasingly from clients. So, could you highlight ESG attributes of Encompass and what criteria you think are most important? Obviously, the server – the vision of your business is, in part, taking care of vulnerable patients as they recover. But I just think it'd be a good form for you to address this, Mark.

<A – Mark Tarr – Encompass Health Corp.>: Now that, well, first of all, it's a priority for boards, a priority for the senior management team [indiscernible] (27:50). And it's been – for the last several years now, it has been a routine discussion point with our board. And we are proud of the fact that, as you know, a primary objective of our organization is to treat the senior population and allow them the ability to stay at home and as independent as they can.

From an environmental standpoint, we consider those factors. When we build and design our hospitals, we run efficient, smaller-sized scale hospitals that are more efficient than larger plans. Certainly, through our supply chain, we've made as many considerations as we can with regards to the environment. With regards to just overall being a good corporate citizen in the communities we serve, you would see that we financially support and are involved in a number of charitable organizations across the board.

And from a governance standpoint, we have a top notch compliance program that reaches all aspects of our organization. So, we're proud of where we are with ESG as a priority. If you look on our website, we have a considerable amount of additional information under the sustainability

portion on our portal. So, we – like I said, we're very proud of where we are with our ESG accomplishments.

Matt Larew, Analyst, William Blair & Co. LLC

Okay. Well, that's great. Mark, Doug, Barb, and Crissy, thank you for your time today. To the audience, thank you for being with us today, and hope everyone has a productive rest of the conference. Thanks.

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

All right, Matt. Thank you.

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