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Encompass Health Corp. (EHC)

Q2 2026 Earnings Call

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

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

Patrick W. Tuer
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OTHER PARTICIPANTS

Pito Chickering
Analyst, Deutsche Bank Securities, Inc.

Matthew Gillmor
Analyst, KeyBanc Capital Markets, Inc.

Ann Hynes
Analyst, Mizuho Securities USA LLC

Whit Mayo
Analyst, Leerink Partners LLC

Ryan Langston
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Brian Tanquilut
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Jared Haase
Analyst, William Blair & Co. LLC

Raj Kumar
Analyst, Stephens, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to Encompass Health Second Quarter 2026 Earnings Conference Call. At this time, I would like to inform all participants that their lines will be in 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 will now turn the call over to Mark Miller, Encompass Health's Chief Investor Relations Officer. Please go ahead.

Mark Miller

Chief Investor Relations Officer, Encompass Health Corp.

Thank you, operator, and good morning, everyone. Thank you for joining Encompass Health second quarter 2026 earnings call.

Before we begin, if you do not already have a copy, the second 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'll make forward-looking statements, such as guidance and growth projections, which are subject to risks and uncertainties, many of which are beyond our...

[Technical Difficulty] (00:01:18 – 00:09:45)

Douglas E. Coltharp

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

Good morning, everyone. This is Doug Coltharp. We apologize for the technical difficulties we're experiencing this morning. These difficulties are arising through our vendors, a vendor we have historically used, and these are not on the Encompass Health side. We appreciate your patience. And with that, we are going to start from the top, assuming that you've heard nothing from us this morning, and I'm going to ask Mark Miller to begin.

Mark Miller

Chief Investor Relations Officer, Encompass Health Corp.

Thank you, Doug, and good morning, everyone. Thank you for joining Encompass Health's Second Quarter 2026 Earnings Call.

Before we begin, if you do not already have a copy, the second 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, such as guidance and growth projections, which are subject to risks and uncertainties, many of which are beyond our control. Certain risks and uncertainties, like those relating to regulatory developments as well as volume, bad debt, and cost trends 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, the Form 10-K for the year ended December 31, 2025, the Form 10-Q for the quarter ended March 31, 2026, and the Form 10-Q for the quarter ended June 30, 2026, when filed. We encourage you to read them.

You are cautioned not to place undue reliance on these 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, 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.

With that, I'll turn the call over to President and Chief Executive Officer, Mark Tarr.

Mark J. Tarr

President, Chief Executive Officer & Director, Encompass Health Corp.

Thank you, Mark, and good morning, everyone. We're very pleased with our second quarter results. As revenue grew 9.6%, adjusted EBITDA increased 9.2%, and adjusted EPS increased 10.7%. Based primarily on our Q2 results, we are again raising our guidance for 2026. Doug will review the details in his comments.

Patient outcomes were again outstanding. Our Q2 discharge-to-community rate was 84.7%, discharge-to-acute rate was 8.4%, and discharge-to-skilled nursing facilities was 6.1%. Our performance on each of these quality metrics continues to exceed industry averages.

We again experienced increased participation in our clinical staff professional growth and development programs, such as our career ladders, providing nurses with support to attain advanced licenses and certifications, including certified rehabilitation RN designation. We believe our success in these programs contributes to our favorable clinical staff turnover trends and helps to drive further declines in premium labor spend. Our professional growth and development programs also enhance our abilities to serve high-acuity, medically complex patients.

Demand for inpatient rehabilitation services remains strong, and we continue to invest in capacity additions. In Q2, we opened a new 50-bed hospital in Concordville, Pennsylvania, and a 40-bed hospital in Loganville, Georgia. Our Loganville hospital is our eighth joint venture with Piedmont. We also added 10 beds to existing hospitals. Through the first-half of the year, we opened three hospitals with a total of 139 beds and added 54 beds to existing hospitals. Over the balance of the year, we intend to open five more hospitals with a total of 250 beds and add 100 to 150 beds to existing hospitals.

We maintain an active pipeline of new hospital development projects, both wholly-owned and joint ventures, while also executing on bed expansion opportunities as warranted by occupancy trends and market dynamics. Our pipeline of announced new hospital projects with opening dates beyond 2026 currently consists of 13 hospitals with 606 beds, and we anticipate additional projects, including small format hospitals, will be announced over the balance of the year.

Last month, North Carolina repealed its Certificate of Need law for inpatient rehabilitation care effective October 1 of this year. We believe this is a great result for the citizens of North Carolina who will now benefit from more access to inpatient rehabilitation care. North Carolina exhibits highly favorable population growth and demographic characteristics, and our assessment points to a large underserved market for IRF services. We currently operate one hospital in North Carolina.

Replicating our approach to seal and repeal in Florida, in anticipation of the CON revocation in North Carolina, we conducted a thorough market-by-market analysis across the state. This has led to an initial prioritization of 15 markets, and we currently have three real estate parcels under contract. We anticipate our next hospital opening in North Carolina to occur in late 2028 or early 2029.

Finally, on July 30, 2026, CMS released the 2027 IRF final rule, which we estimate will result in approximately 2.3% increase in net revenue per discharge for our Medicare patients beginning October 1 of 2026, based on our current patient mix.

Now, I'll turn it over to Doug.

Douglas E. Coltharp

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

Thank you, Mark, and good morning, everyone. Q2 revenue was up 9.6% over the second quarter of 2025. The increase was comprised of 5.6% discharge growth and a 3.9% increase in net revenue per discharge. Net revenue per discharge growth was driven by higher patient acuity. We continue to see very solid growth in medically complex categories, including stroke and brain injury.

Bad debt expense in Q2 was 2.3%, in line with our expectations, and the increase over last year is primarily due to a favorable reserve adjustment that occurred in the second quarter of 2025. Our Q2 adjusted EBITDA increased 9.2% to $348 million, even as we absorbed an $11.5 million year-over-year decrease in net provider tax impact.

Essentially, all of the year-over-year change in net provider tax impact relates to out-of-period adjustments to our accruals for the fiscal year 2025 Florida Medicaid program, based on revisions promulgated by the state and approved by CMS in Q2 of this year. Q2 SWB per FTE increased 3.4%, in part driven by increased participation in our career ladder programs, partly offset by a decline in premium labor. Premium labor costs, comprised of contract labor and sign-on and shift bonuses, declined $2.6 million from Q2 2025 to $25 million.

Contract labor FTEs as a percent of total FTEs was 1.1%, an improvement of 20 basis points from Q2 2025. Net pre-opening and ramp-up costs were $6.9 million, up $2.9 million from Q2 2025, and were $10.9 million on a year-to-date basis, compared to $6.1 million in the first-half of 2025.

We continue to expect net pre-opening and ramp-up costs of $18 million to $22 million for the full-year. During Q2, we repurchased approximately 704,000 shares of our common stock for a total of $74.2 million, bringing our year-to-date total share repurchases to approximately 1,412,000 shares and $145.8 million.

During Q2, we issued $500 million of 5.875% senior notes due 2034 and used most of the proceeds from that issuance to redeem $400 million of our 4.5% senior notes due in 2028. Our net leverage at quarter end was 1.9 times. Our leverage and liquidity remain well-positioned. We recently announced an increase in our quarterly dividend, next payable in October, to $0.21 per share. And within our earnings release yesterday, we announced an increase in our common stock repurchase authorization to $1 billion.

As Mark mentioned, we have again raised our 2026 guidance as follows. We now expect for the full-year net operating revenue of $6.41 billion to $6.49 billion, adjusted EBITDA of $1.365 billion to $1.395 billion, and adjusted earnings per share of $6.02 to $6.25. The considerations underlying our guidance can be found on page 11 of the supplemental slides. And I want to take just a moment to highlight updated assumptions.

Our Medicare pricing assumption for Q4 of approximately 2.3% reflects the IRF final rule released on July 30. Our revised expectation for full-year 2026 SWB per FTE growth is 3.5% to 4%, as we expect increased participation in both our nursing and therapy career ladder programs. As we have previously stated, we believe these programs contribute to favorable clinical staff retention trends, higher quality patient outcomes, and reduced reliance on premium labor.

We previously indicated that we expected the net provider tax impact to adjusted EBITDA for 2026 to be essentially flat with 2025 at approximately $21 million. Based on the retroactive adjustments specific to Florida that I mentioned earlier, we now expect the net benefit to adjusted EBITDA in 2026 to be approximately $10 million.

And with that, we will open the lines for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And we'll take our first question from Pito Chickering with Deutsche Bank. Your line is now open.

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

Morning, Pito.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Morning, Pito.

Pito Chickering
Analyst, Deutsche Bank Securities, Inc.
Q

Hey, good morning, guys. Thanks for taking my questions. And nice job getting this earnings call going this morning.

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

We didn't know it was going to be so hard, Pito.

Pito Chickering
Analyst, Deutsche Bank Securities, Inc.
Q

So, look, you raised the guidance the back-half of the year by about $5 million, despite assuming 10 basis points of lower Medicare pricing in the fourth quarter. In [ph] SWB (00:23:37), that's 500 basis points higher than you had

assumed previously. So can you bridge us, the good guide, the back-half of the year versus last quarter to help understand how you got so much leverage to raise EBITDA despite those two macro pressures?

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

Yeah, Pito, this is Doug. I'll take a shot at it. So, we had some favorability in the second quarter and really for the first-half in a couple of areas. One is pricing, which was driven predominantly by patient acuity. There's no certainty that that continues into the second-half, but it does represent a source of potential upside. Additionally, we did see some further benefits in EPOB. Some of that is attributable to the fact that we've been running at a higher year-to-date occupancy level, and I can go through some of that if you'd like. And it's also an ancillary benefit related to the career ladder program participation.

And again, the causality there is we believe that the career ladder program participation is contributing to favorable clinical staff turnover. And when you've got favorable clinical staff turnover, that means that your new hires can consequentially come down, which means that you're spending less hours that would get into the EPOB calculation during orientation.

Pito Chickering
Analyst, Deutsche Bank Securities, Inc.
Q

Okay. Fair enough. And then can you talk about the same-store discharge growth in the quarter, the durability of that strength? Just as you think about the second quarter 2026 stacked comps heading into easier comps in the back-half of the year, just be modeling more same-store discharge growth in the 4%-plus for 3Q and 4Q? Thank you.

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

Yeah. So again, this is a statement you've heard us made repeatedly for the last several quarters, but we believe increasingly that the distinction between same-store and total discharge growth is going to come less relevant and less consequential. We are up against easier comps in the second-half of the year, and so that will be favorable. We also anticipate that the impact of the four-unit closures that we had beginning in June of last year will dissipate a bit further. But we've got a lot of new capacity coming on in the second-half of the year. It is skewed more heavily towards Q4 than Q3, but that will be a contributor, to some extent, for total discharge growth as well.

Pito Chickering
Analyst, Deutsche Bank Securities, Inc.
Q

Great. Thanks so much.

Operator: And we will take your next question from Matthew Gillmor with KeyBanc. Please go ahead.

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

Morning, Matt.

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

Hey, Matt.

Matthew Gillmor
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey. Good morning, guys. Thanks for the question. Maybe following up on the North Carolina comments. I think you had mentioned there's 15 markets you're prioritizing. I was curious what you thought the overall opportunity is in North Carolina? And would that be enough to impact your de novo target of six to 10 per year, or just maybe bias you towards the high end as you're thinking about beyond 2027?

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

A

Yeah, this is Doug. I think, right now, if we could get 15 open, we'd feel pretty good about that, but that certainly doesn't mean that the opportunities in the state of North Carolina would be exhausted at that level. And I should note that that 15 is looking at markets both large and small as well. There are good pockets of opportunity really dispersed across the state, which is very exciting to us.

I think at a minimum, it would drive us probably beginning in 2029 towards the high end of that six to 10 range, and there is some possibility just on how quickly we can pull those together, as well as some opportunities that continue to develop in other states that we could wind up going above that. But right now, we're going to stay with the six to 10 range and hope that North Carolina pushes us to the upper end.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

Matt, this is Pat. One additional point that I'd make there is as we get the small format hospital concept up and rolling, that'll provide substantial opportunity and runway for us to continue to grow in North Carolina beyond just the traditional de novo format.

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

A

And I think, to piggyback on what Pat said, we've talked before about one of the benefits of the introduction of small format hospitals, that allows us to approach certain markets with a hub and spoke type strategy. And given that we only have one hospital in the state of North Carolina and the extensive opportunities that are there, we're essentially starting with a blank sheet of paper. And so really utilizing the combination of de novos and small format hospitals to pursue that hub and spoke strategy in that market could be very compelling.

And that's why you may not see it push the number of de novos up, but I think what will become increasingly important, and we'll be able to provide some more visibility on this as we move into 2027, is what do we think is the opportunity for total beds to be added to the state?

Matthew Gillmor
Analyst, KeyBanc Capital Markets, Inc.

Q

Great. And then as a follow-up, I wanted to ask about the payer denial topic. There was an OIG report that highlighted the wide variation in denial rates among MA plans for IRF services. I was curious what your reaction was to that report? And I also wanted to see if there were any early learnings from the admit and appeal strategy that you'd discussed on prior calls?

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

A

Yeah. So I would say just in general, that the denials through pre-authorization from Medicare Advantage continues to be a challenge. The trends that we saw in Q2 were not really dissimilar. We saw some marginal improvement from what we experienced in Q4 of last year and Q1 of this year, but there remains a very substantial disparity between what we see out of the MA plans and Medicare fee-for-service patients.

Now, we understand, from the comments made by large MA providers, that they are struggling to achieve what they deem as an acceptable level of profitability. But denying access to appropriate care for Medicare beneficiaries is not the right solution to that. We are very pleased with what we have seen thus far in the pilot program. And again, that's our admit and appeal strategy. We initiated that with select patients across nine of our hospital markets towards the end of February. So it remains fairly early in the program. And remember, there are five various levels of appeal that you can go through. I won't take you through each of those five right now.

Through the end of July, we had a total of 298 patients who had been admitted into our hospitals on that basis. 144 of those have been fully adjudicated, and of that 144, we have prevailed on 128, which is an 89% success rate. And I'll turn it over to Pat to maybe comment about how we see potential opportunities to extend that program in the future.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Thanks, Doug. I think the first opportunity for us to scale this up – within that 89%, there's certain diagnosis that are almost 100% or darn close to it. And I think as we think about scaling, it'll likely be within those diagnosis categories that we move forward across the portfolio and then evaluate fully scaling the rest of the program up.

But we're in conversations and evaluations of the education program and rollout that'll have to take place for that to happen. And that's something we're preparing for now. But a broader rollout of the whole program, I think we still want to get some more time under our belt, bigger sample size, but there's certain things right now that we think have the potential to be scaled throughout the portfolio.

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

Now, we've talked in the past about just the stroke program in general and how we had – some of the payers seem to recognize the value proposition around the stroke patients more so than others. And that would certainly be one of the diagnostic categories that Pat had mentioned that would be a likely candidate to try to push forward.

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

And when you're prevailing at almost 90% on these patients, what it tells you is that those patients should have been admitted on the front end into our hospitals. And the fact that we have to go through this admit and appeal strategy is doing nothing but adding to the cost of the healthcare system by increasing the administrative costs.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Yeah. I think just to put a bow on this. I think you could see that we'll look to scale certain parts of this in the coming quarters, and then by the end of the year, I think we'll be in a position to evaluate for a full, broader rollout across the company.

Matthew Gillmor
Analyst, KeyBanc Capital Markets, Inc.

Q

Great. Thank you.

Operator: And we will move next to Ann Hynes with Mizuho Securities. Please go ahead.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

Morning, Ann.

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

A

Hey there, Ann.

Ann Hynes
Analyst, Mizuho Securities USA LLC

Q

Great. And good morning. Thank you. So I guess my first question is, you announced a nice share repurchase program this morning. How do you view that versus your other capital needs going forward? And I did notice that year-over-year, you have, I think it was a 20% increase maybe in CapEx year-over-year. And what is driving that? Is this an acceleration of development versus last year?

And then, thanks for all the detail on South Carolina. I know that's a CON you've been waiting for, but I believe there's two other states, I think it's North Carolina and Tennessee, that could be expanding CONs for inpatient rehab. Any updates on those? Thanks.

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

A

Yeah. So it's North Carolina. South Carolina did not – South Carolina was previously repealed. And we have a much larger presence. What do we have? 11 hospitals in South Carolina already. We do hear that there is some dialogue around Tennessee. And don't know that anything is imminent there. But we continue to have good success getting CONs approved in Tennessee and have a couple of opportunities that are already in the pipeline there. Nothing else from a CON repeal perspective that is currently viewed as imminent.

In terms of CapEx, going in reverse order here. Yeah, CapEx this year is running right at about 15% of revenue. We think that probably represents close to a high watermark. Most of the increase on a year-over-year basis is in capacity expansions, which is a good thing. And again, some of that is directly related to those high occupancy doors we referenced in Q1 and our ability to add beds there, as well as what remains a robust de novo pipeline. And then as Pat alluded to previously, we're really excited about the introduction of the small format hospitals with the intent to get at least one open next year and then increase that to close to a handful, at least, on an annual basis beginning in 2028.

The story on capital allocation, the increase in the share repurchase authorization notwithstanding, remains unchanged. And we like to say that we're an and story, not an or story. Because of the strength of our free cash flow and the resulting strength in our balance sheet, we have the capacity to increase the capital expenditures and increase the number of beds that we're adding to our overall franchise on an annual basis. But augment that with the dividend, which was increased for the October payout, and increasingly with share repurchase activity.

Ann Hynes
Analyst, Mizuho Securities USA LLC

Q

Thank you.

Operator: And we will move next to Whit Mayo with Leerink Partners. Please go ahead.

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

A

Morning, Whit.

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

A

Hey there, Whit.

Whit Mayo
Analyst, Leerink Partners LLC

Q

Hey, guys. Mark, you've talked a good bit on this call about various investments in workforce development that you guys are making. Do you have any numbers that you could share around turnover, employee satisfaction, anything to gauge the impact that these investments are making?

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

A

Yeah, we do. I'm going to let Pat go into greater detail on that. But just a quick comment on the clinical ladders. That's not a new tool, but we have a team that did a really nice job going in, back in to look to see what appeals to the clinical workforce, updated things. We've promoted it internally, and we've had a really good response, which is definitely impacting our turnover rates. It's impacting our ability to not only retain staff, but it's affecting our ability to hire staff in both existing hospitals and to staff up our de novo hospitals. So , Pat, you want to give some details around that?

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

Yeah, sure, Mark. So on an annualized basis through Q2, our nursing turnover sits around 19%. That represents a low of 12-plus years. On the therapy perspective, we're just above 7%. That's our lowest turnover on an annualized basis in five years. So really pleased with the progress there.

From a ladder perspective, we are up to 43% of eligible RNs and certified nurses that are participating on the ladder. If we think about the turnover within that group, it's only 5%. If they're a non-laddered nurse, the turnover is closer to 25%. If we can get a nurse certified, even if they're not on the ladder, turnover is only 12%. And we've increased the number of certified nurses by almost 21% versus prior year, and 60% since 2023.

So these programs are certainly having the intended outcome in terms of producing lower turnover, lower premium pay costs, the benefit to EPOB, and lower unproductive time, as well as allowing us to build enhanced clinical capabilities and fueling the value proposition through strong outcomes. We're pretty excited about this.

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

You know, Whit, if somebody puts in the time and effort to get their CRRN, there's a pretty good chance they're going to stay in rehab as opposed to going out and trying other specialties. And as we've noted, these are increasing their clinical skills, which ultimately allows us to take medically complex patients, and it's just been proven out. So it really seems like a lot of things are clicking on all cylinders around this initiative.

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

We currently have approximately 22% of our RNs have the CRRN certification. That does carry a premium in terms of their wage rate. It's about 9% over their peers who do not have that certification. But as Pat just enumerated, we think that the benefits are more than offsetting.

Whit Mayo
Analyst, Leerink Partners LLC
Q

All right. And maybe my follow-up, just wanted to get an update on the VA initiative and whether that's having any meaningful contribution to same-store growth? Thanks.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Yeah, Whit, thanks for teeing that up. That remains a source of pride for us and a very fulfilling patient population for us to serve. This is the first quarter where we've really anniversaried a lot of the growth that we had in the VA program that we started talking about last year. And in Q2, we hit VA growth of around 33%. It now represents about 23%, just under 23%, of our managed care volume, and there still is a lot of runway there.

Our local teams and our regional teams have done a really nice job collaborating with the VA populations within their markets. And you may recall, we have talked about that there's 8 million veterans over the age of 65 in the country, and we're on pace to treat somewhere close to 10,000 by the end of the year. So substantial runway there.

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

And as a reminder, that pays at the Medicare fee-for-service rate.

Whit Mayo
Analyst, Leerink Partners LLC
Q

Right. Appreciate it, guys.

Operator: And we will move next to Ryan Langston with TD Cowen. Please go ahead.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Morning, Ryan.

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

A

Hello, Ryan.

Ryan Langston
Analyst, TD Cowen

Q

Good morning. Maybe I missed this. I got dropped from the call, unfortunately. But maybe just an update on the recently opened facilities versus the bed additions over the last year? And maybe how each of those cohorts have been ramping versus your historical average?

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

A

Yeah. I think the bed additions and the de novos continue to ramp very favorably. If we look at the openings on a year-to-date basis, in Q1 we opened one hospital with 49 beds. In Q2, we opened two hospitals with a total of 90 beds. From a bed expansion perspective, in Q1 we added 44 beds, in Q2 we added 10 beds. Those 10 beds, importantly, were added to three of the hospitals that in Q1 had an occupancy level of north of 95%.

As we've stated previously, the returns on our de novos are in part driven by the fact that we had – tend to experience a very rapid ramp-up in those. On average, our de novos achieve four-wall positive EBITDA by the time they hit month six, and they're typically north of the 70% occupancy rate by the time they get to month 10.

Now, those are averages, so some are faster and some are slower. But we think that over the years that we've been pursuing an accelerated de novo strategy, which really came to fruition in 2021, we have further refined our processes. We've set up dedicated teams across functions to do nothing but open the de novos. And as a result, the progress that we're making from the day that we open the doors has really improved and has increased the time to achieving four-wall profitability.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

One thing I would add to that is, just as we think about bed additions, and last quarter, we talked a lot about the capacity-constrained hospitals, and the cohort that represented that. We have lowered the threshold of when we start the evaluation process for bed additions, just to try to time that capacity coming online to when we actually need it, so we're not missing out on potential volume. So we, again, have lowered that threshold to 70% to 75% versus the historical 80% to 85% threshold.

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

A

Ryan, I'd also say it's been really nice to see the ramp-up momentum in hospitals, not only, like, in the state of Florida, where we have a well-known brand, but as we've gone out into new states, Connecticut, we opened up in Rhode Island a couple of years ago. Those are markets where you will have to do a lot of education about IRF versus SNF, and it's been really nice to see the ramp-up in these new markets to complement the states where we already have a strong presence.

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

A

And I think it's important to note that the increase that we've been experiencing over the last several years in system-wide occupancy is an important driver of efficiency. And you're seeing that flow through the P&L.

And to put a finer point on that, our Q2 occupancy of 77.4% was up 290 basis points over Q2 2025. And sequentially, occupancy decreased only 130 basis points from Q1 of this year, and that compares to a decrease of 220 basis points from Q1 to Q2 in each of 2025 and 2024. And further, our average daily census, or ADC, decreased only 69 from Q1 as compared to a sequential Q1 to Q2 decrease, in ADC of 184 in 2025 and 113 in 2024. Q1 and Q2 also represented the first two quarters in company history with ADC in excess of 9,000.

Ryan Langston
Analyst, TD Cowen

Q

Great. Appreciate all the detail. Just a quick follow-up maybe to Ann's question on share repurchase. How should we think about you utilizing this over time? I don't think the EPS guidance change implies a material increase in repurchase through the back-half of the year. But any reason we shouldn't think that this could ramp-up at least versus the first-half? Thanks.

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

A

Yeah. The EPS guidance change reflects only the share repurchases that had been accomplished year to date. I think you have seen an increase the last three quarters from our historical run rate in share repurchase. We continue to have capacity in the balance sheet based on the leverage ratio that we're running, and also then we have capacity just given the free cash flow and the relationship of that free cash flow to our growth CapEx number as well. So clearly there's capacity for increased share repurchase activity in the future, and if that had not been the case, I don't think the board would have taken the action of increasing the authorization.

Ryan Langston
Analyst, TD Cowen

Q

All right, guys. Thank you.

Operator: And we will take our next question from Joanna Gajuk with Bank of America. Please go ahead.

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

A

Morning, Joanna.

Joanna Gajuk
Analyst, BofA Securities, Inc.

Q

Hi. Good morning. Thanks so much. So couple of questions. So first, I guess on the volume discussion, and you mentioned that you're seeing higher acuity. And I guess in the past, you gave us these stats. I haven't heard them in a while. So I want to ask, can you give us some of these growth rates by category, like the stroke, neuro, brain injury versus ortho or, hip and knees?

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

A

Yes, we can do that.

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

I can touch on that to start. Two of the largest categories of growth for us were in stroke and brain injury. Those were up 7.9% and 8% respectively, on a same-store basis, 5.5% and 3.9% respectively. Brain injury has been a – we talked about this on the last call, probably the call before that as well. We continue to see a lot of growth in brain injury, specifically non-traumatic brain injury, which from a claims perspective, represents the largest source of potential market capture for us. So it's great to see us capitalize on that.

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

Yeah. I think you asked specifically about lower extremity joint replacement. Knee and hip replacement, which is how we categorize that, was up only modestly about 1% in the quarter.

Joanna Gajuk
Analyst, BofA Securities, Inc.
Q

Okay. Great. Yeah. That's what I was getting at. So clearly, these other categories, higher acuity, growing much faster than orthopedics. So thanks for that. And if I may, a follow up, in terms of the – I guess de novo and the plans adding beds and such, and as it relates to the pent-up demand, can you give us the stat you gave us last quarter in terms of percent of your hospitals that are above 90% occupied? And to that end, can you talk about the bed expansions or de novos, right? And how much, I guess, you achieved in terms of capturing the pent-up demand in those hospitals you called out prior to that quarter? Thank you.

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

Yeah, absolutely. So in Q1, we had 65 hospitals with occupancy rates greater than 90%, and an average in that cohort of 95%. In Q2, we had 60 hospitals at greater than 90%, so a decrease of five, with an average occupancy rate of 94%. Three of those hospitals that dropped from that cohort did so because of the bed expansions that occurred in the first-half. And approximately 90% of the bed additions that we have in the pipeline and targeted for the second-half of this year and the first-half of next year are going into hospitals that are in that greater than 90% cohort.

Joanna Gajuk
Analyst, BofA Securities, Inc.
Q

Great. Thank you so much. Appreciate it.

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

Again, it's the definition of a high-class problem.

Joanna Gajuk
Analyst, BofA Securities, Inc.
Q

Exactly. No, I love it. Thank you. Thanks so much for taking the question.

Operator: And we will move next to Andrew Mok with Barclays. Please go ahead.

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

Morning, Andrew.

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

Morning, Andrew.

Andrew Mok
Analyst, Barclays Capital, Inc.
Q

Good morning. The same-store discharge growth of 2.8% accelerated 120 basis points sequentially despite tougher comps. One, did that finish better than internal expectations? And if those higher acuity categories that you called out are driving the better volumes and are expected to continue, why is there a hesitation to say that those acuity gains may not be sustainable? Thanks.

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

Yeah. So, first, we're not going to comment on performance versus internal expectations. We, again, will just compare it to guidance, and obviously, we revised our guidance upwards for the full-year based on the second quarter performance. This is, again, one where we continue to believe that the breakdown between same-store and total discharge growth is less relevant because you can be influenced in any particular quarter by bed additions, which go immediately into the same-store count, and also by the maturation of de novos, which were outside of the same-store category into the same-store category. And there are other influences that we've cited previously that can impact same-store discharge growth from quarter-to-quarter.

With regard to the increase in acuity, we think that is very positive. One, because there's a bit of a competitive moat around that. It is a real challenge to treat successfully those more medically complex programs. And we're very proud of the clinical programs that we have in place that allow us to do that. It also creates a competitive advantage because part of the value proposition, a significant portion of the value proposition that we have for our upstream acute care partners, is the ability to take those patients out of their facilities with a lower length of stay in the acute care hospital, which frees up the bed for them.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.
A

Andrew, this is Pat. I don't think it's a reluctance for us to commit to that in the foreseeable future. I think what – from our standpoint, we see fluctuations in acuity from quarter-to-quarter, year-to-year. While we're very confident in the ability for us to capture that market share, I don't think it'd be prudent for us to back us into a corner and then have one of those fluctuations that occur from time to time. But we're very confident in the outcomes that we provide and the access to care that we're able to provide, and our teams do a great job of capitalizing on that.

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

Another factor that can impact the acuity is it's important that we not be perceived by our referral sources as cherry-picking certain types of patients. We can create the most value for our referral sources, the hospitals, and the attending physicians if we're willing to accept all patients who qualify for admission into an inpatient rehabilitation facility, and not just say, we're only going to take your stroke or your brain injury patients. And so

doing that based on the flows that come into an acute care hospital in any particular quarter can cause some fluctuations in that acuity.

But again, when you look at some of the headwinds that are now baked into our guidance, specifically incorporated into the second-half, one of the potential areas of upside that I cited earlier is seeing improved pricing continue for the balance of this year based on some sustainability in that higher acuity.

Andrew Mok
Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

Operator: And we will move next to A.J. Rice with UBS. Please go ahead.

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

A

Morning, A.J.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

Hey, A.J.

A.J. Rice
Analyst, UBS Securities LLC

Q

Hi, everyone. First, just wanted to ask about one more question on the career ladder and the decision to boost your SWB expense growth by 50 basis points. Is that – should we think of that as this year only, or are you trading off higher wage growth on an ongoing basis for better turnover and then the back-end benefits of that? How should we think about this?

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

A

Yeah. I think right now it is an assumption for this year only and specifically for the back-half trend. We believe that as we move, just because of the success we've had in the participation in these ladders on a year-to-date basis, as we move into next year, we would expect to start anniversarying some of those increases. And so we should see the SWB per FTE moderate that, but we're not ready to call a level on it yet.

And remember, as we move into the second-half of this year, we're also up against easier comps, or excuse me, tougher comps in terms of more favorable outcomes from last year. If you look at Q3 of 2025, SWB per FTE inflation was 2.6%, and in Q4 it was 2.1%. That compares to 3.2% in Q1 of 2025 and 4% in Q2 of 2025.

A.J. Rice
Analyst, UBS Securities LLC

Q

Okay. Yeah, no, that's helpful. I just wondered also, any update on your technology investments and AI initiatives? I know you have called out previously a partnership with Palantir around claims processing and on the administrative side. Are you seeing any meaningful efficiencies yet, or is that mostly still in front of you?

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

A

I think a lot of it is still in front of us, but we've definitely seen many enhancements in our processes. Both – there's a lot of AI that is now embedded as an aid or a tool in our clinical workflows that aid the patient journey. Everything from the pre-screen narrative to automation of the face-to-face notes. We've used it to enhance our falls risk model, our react model, and our readmission model. We've spoken previously about the agentic solution we have, which we call [ph] Hannah (00:54:22), for following up with recently discharged patients.

On the administrative side, it really runs the gamut from agents that are helping us with the monthly closing of the books and scanning journal entries for exceptions. We referenced previously that what is coming soon is going to be an enhanced market analytics tool that's really going to help us devise the appropriate real estate strategy for markets that we're entering. We think it's going to be very useful as we map out our strategy for North Carolina. So there's a lot in the pipeline.

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

A

But I will say, A.J., we've got a team that's been very intentional in terms of prioritizing projects and initiatives in which we wanted to work with Palantir. So we're looking for those that can benefit us the greatest in terms of either efficiencies or working through projects like the development of opportunities and evaluating markets.

So I'm with Doug. I think that the benefits still are out in front of us, but I'm very encouraged about where we are and probably more importantly, how we're going about it as an organization.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

A.J., this is Pat. Just a couple of other call-outs from a use case perspective that I'm pretty excited about, in addition to the ones that Doug talked about. One of the challenges that we have from an operations perspective is when we are manually auditing records and clinical systems, it takes a lot of time, it takes a lot of effort, it takes a lot of resources. And we're developing a solution with Palantir and our ITG team, our internal IT team, that will proactively and concurrently scan our medical records for any potential risk area. If an order is not followed or if an order is delayed, and you can act and intervene in real time. So I'm pretty excited about that.

And then, not specific to Palantir, but we did talk in prior calls about our Fusion ERP conversion, we've gotten our sea legs under us with that. We continue to enhance that system, and we're evaluating opportunities that may come with that to centralize certain tasks that could reduce or create efficiencies for us in the near future. We're just not ready to call those out just yet.

A.J. Rice
Analyst, UBS Securities LLC

Q

Okay. Thanks.

Operator: And we will take our next question from Brian Tanquilut with Jefferies. Please go ahead.

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

A

Hey, Brian.

Brian Tanquilut
Analyst, Jefferies LLC

Q

Hey, guys.

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

A

Morning, Brian.

Brian Tanquilut
Analyst, Jefferies LLC

Q

Good morning. Congrats on the quarter. Maybe, Doug, as I think about temp staff or contract labor utilization, obviously down a decent bit during the quarter, just curious how we should be thinking about the back-half, especially in light of planned openings coming up in the pipeline?

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

A

Yeah. So we've historically been very good about not having to tap into contract labor for de novo openings, and we would hope that will continue to be the case in the second-half. We're really proud of the progress that we have made and that we continue to make on decreasing the utilization of premium labor. Q2 marked our 11th consecutive quarter where we had a year-over-year decline in premium labor cost, even as over that period of time, our volume has increased substantially.

But being at 1.1% of total FTEs in contract FTEs, and the fact that the rate has really stabilized for about a two-year period right now at an annual rate of about $175,000, we've kind of hit the point of diminishing returns. So part of what's embedded in the increased assumption for SWB per FTE, the inflation rate there for the second-half is just that realization that incrementally, we would hope to continue to improve, but the level of improvement is going to be less than it has been for the last almost three years.

Patrick W. Tuer
Chief Operating Officer & Executive Vice President, Encompass Health Corp.

A

Just to add to that, this is Pat. Doug's right. There's some diminishing returns on this, but there is still juice left to squeeze here. Again, it's just going to be smaller than what we have been able to produce over the last several quarters sequentially.

A couple of call-outs. In January, we started a pilot with our top 10 markets from a contract labor, extra shift and sign-on perspective that had historical recruiting challenges. And we worked with our talent acquisition team and our regional operators and piloted a partnership around recruitment marketing. And we saw a substantial improvement in the majority of those markets, way over the historical hiring trends that had occurred, and we saw nice reductions there.

Some of those markets are still going to see continued improvement, which we will benefit from. And then there's opportunities for us to take that pilot to other markets that are challenged as well. And then I'll just call out that this was our best hiring quarter that we've had in some time, and that comes off of a really strong Q1. So I know that, that can change year-over-year, but right now, from a labor availability perspective, it's probably the least stressed that I've been about it in several years.

Brian Tanquilut
Analyst, Jefferies LLC

Q

That's awesome. And then, Doug, I noticed the new slide added there, slide 19 for the RCD and TEAM. Just curious, anything you can share with us in terms of what you're seeing with RCD at this point? Thank you.

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

A

Yeah. So I would say, things continue to be about the same in Alabama. We're above – for all seven of our hospitals, we're above the target affirmation rate, which is north of 90%. The rollout in Texas has gone very well, and there we're seeing affirmation rates that are consistent with what Novitas had demonstrated in Pennsylvania previously of north of 98%.

California, which is a smaller number of our hospitals, I would say that the MAC was less well-prepared than we would have hoped for, but they're continuing to make some progress. We're above the target affirmation rate there, and we would expect continued improvement. We don't really see any reason why that should differ from the experience that we've been having in the state of Texas.

And then finally, the inclusion of our hospitals in Pennsylvania has been deferred for a period of time, but we will have a couple of hospitals in Pennsylvania that we believe will be subject to RCD, beginning in 2027. The experience for other providers in the state of Pennsylvania thus far has been positive. And so we're optimistic about that as well. And then we're not currently aware of plans by CMS to extend RCD into any other states at this time.

Operator: And we will move next to Jared Haase with William Blair. Please go ahead.

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

A

Morning, Jared.

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

A

Morning, Jared.

Jared Haase
Analyst, William Blair & Co. LLC

Q

Morning. Thanks for squeezing me in here. Maybe I'll just stick with one, as we get towards the end of the call. I wanted to go back on the career ladder programs and appreciate the investment that you're making there. I wanted to sort of try and connect that back to the model a little bit.

So when I think about the dialogue that you have with referral partners to drive volumes, are you actually able to articulate some of that data around, let's say, the tenure of your workforce, the mix of credentials, turnover rates, things like that directly? I sort of get ultimately, at the end of the day, quality measures, readmission rates are probably the main things that they're going to focus on. In some sense, that's basically downstream from the quality of our workforce. So just trying to get a sense of how that actually plays out in the go-to-market as you try to capture volume?

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

Yeah, Jared, I think those conversations directly around turnover and the improvements to the overall business are more direct with our joint venture partners, than they are non-partners. I think for non-partners and joint venture partners, the primary focus comes down to outcomes and how fast can we take their patients.

And if we have a more stable, trained clinical workforce, we're able to do those – take a wider variety of conditions and take them sooner before certain conditions can resolve and reduce acute length of stay and associated readmissions. So that's really where the conversations come in. But again, from a partner perspective, they're very interested in those labor dynamics as it has a direct line to their distributions.

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

I would also say that the more skilled and more tenured your clinical workforce is, there's a correlation of that to your ability to obtain at a hospital level, disease-specific certifications. And when we can go to a referral source citing the disease-specific certifications that we have, and then providing them with our clinical outcomes, that presents a very compelling case.

Jared Haase
Analyst, William Blair & Co. LLC
Q

Okay. Very helpful. I'll leave it there. Thank you.

Operator: And we'll take our next question from Raj Kumar with Stephens. Please go ahead.

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

Morning, Raj.

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

Hey, Raj.

Raj Kumar
Analyst, Stephens, Inc.
Q

Hey, good morning. Maybe just going back to the North Carolina opportunity, I guess, curious on that front, how you see it in terms of JV versus wholly-owned? And then I thinking as a Florida as a use case, maybe illustrating the kind of ramp in that state and what the timeline looks like to reach your targeted market share or, saying getting your fair share from acute admissions, in that market?

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

I'll take the first part of that. I mean I think that North Carolina will be like what we've seen in other states. It'll be a combination of some wholly-owned hospitals and some JV partnerships. Our existing hospital in Winston-Salem is a partnership with the Novant system. So I think that as we initially look at these 15 markets, we see some that

may be more likely to be partnered than others, just given the dynamics in the marketplace. But I think you could count on a mixture of some wholly-owned and some joint venture facilities within the 15 markets.

Douglas E. Coltharp

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

A

There are a number – any number of benefits that are attendant to a joint venture versus a wholly-owned. One of them is the ability to get a CON foothold in a state because the acute care partner is already established by definition, and we may be new to that market or to that state in particular. That doesn't apply when you've got the CON barrier removed.

So there are some analogies to Florida, but some distinctions as well. If you think about it, when the CON was revoked in Florida, we already had presence with 12 existing hospitals. So we were well known to many of the acute care providers, and that facilitated more of a balance of joint ventures and wholly-owned. And that's a little bit distinct from North Carolina, where we have just one, even though it isn't a joint venture.

Where you get a more parallel path, though, is that we felt that first-mover advantage was extremely important, and we can move faster alone than we can negotiating joint ventures on the front end. So with the expansion in Florida, what you saw us do was go out and initially move with a portfolio approach that was much more balanced towards wholly-owned than joint ventures. But as we got along the way and announced certain projects, a number of those that started as wholly-owned converted to joint venture opportunities. And I would expect a similar type of trajectory in North Carolina.

We're prepared to move quickly, and start projects, and we're going to do that. And once those projects are announced, we'll survey the market and make a determination as to whether or not that particular project would benefit from the presence of a joint venture partner.

Raj Kumar

Analyst, Stephens, Inc.

Q

Great. I'll leave it there. Thanks.

Operator: This concludes the Q&A portion of today's call. I will now turn the program over to Mark Miller for closing remarks.

Mark Miller

Chief Investor Relations Officer, Encompass Health Corp.

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

Operator: Thank you. This brings us to the end of today's meeting. We appreciate your time and participation. You may now disconnect.