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
Joanna Gajuk – Analyst, BofA Securities, Inc.
Matt Larew – Analyst, William Blair & Co. LLC
Brian Gil Tanquilut – Analyst, Jefferies LLC
Matthew Dale Gillmor – Analyst, Robert W. Baird & Co., Inc.
A.J. Rice – Analyst, Credit Suisse Securities (USA) LLC
Ann Hynes – Analyst, Mizuho Securities USA LLC
Pito Chickering – Analyst, Deutsche Bank Securities, Inc.
Frank George Morgan – Analyst, RBC Capital Markets LLC
Sarah E. James – Analyst, Piper Sandler & Co.
Andrew Mok – Analyst, Barclays Capital, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to Encompass Health Third 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 will 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 third 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; Patrick Darby, General Counsel and Corporate Secretary; and April Anthony, Chief Executive Officer of Encompass Home Health and Hospice.

Before we begin, if you do not already have a copy, the third 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 the magnitude and impact of the COVID-19 pandemic that could cause our 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, 2019, and the Form 10-Q for the quarters ended March 31, 2020 and June 30, 2020, and September 30, 2020 when filed. We encourage you to read them.

You are cautioned not to place undue reliance on 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, reconciliations to the most directly comparable GAAP measures 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.

Before I turn it over to Mark, 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 Mark.

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

Thank you, Crissy, and good morning to everyone. We have a proven track record of working through difficult situations. Since 2009, we have successfully managed through an economic recession, regulatory changes, sequestration, and Medicare payment freezes and cuts. And now, we can add a global pandemic to that list. Our teams are doing an extraordinary job in managing through the various COVID-19 challenges. While our operating environment remains difficult due to the pandemic, we remain confident in the prospects of both of our business segments and in our ability to overcome these challenges. It's what we do. We adapt, we persevere and we continue to grow.

Let's talk first about our inpatient rehabilitation segment. Our inpatient rehabilitation volumes recovered substantially in the third quarter of 2020. While total discharges were down 1.5% compared to the third quarter of 2019, this number improved significantly from the 10.7% decrease in volumes we experienced in the second quarter of 2020. The remaining lag to returning to prior year volumes primarily is related to orthopedic and lower extremity joint replacement cases. Many of our markets continue to have limited elective surgeries, particularly with elderly patients with complex medical conditions. These patients are the ones that tend to need inpatient rehabilitative services post-surgery.

To put this in perspective, same-store discharges for the third quarter of 2020 decreased by 1,311 patients compared to the same period of 2019. In the third quarter, we treated 1,316 fewer orthopedic and lower extremity replacement patients than we did a year ago, accounting for the entire same-store Q3 decline. We also continue to experience COVID-related challenges in certain geographic markets, specifically Florida, where we have 12 inpatient rehabilitation hospitals. We experienced a 12.8% year-over-year decline in patient discharges in Florida in the third quarter of 2020. Factors such as limited elective surgeries and restrictions on when positive COVID patients can be transferred from an acute hospital to a post-acute setting played a significant role in this volume decrease. It's important to remember that these factors are temporary responses to the pandemic and are not indicative of structural shifts in the market.

Net revenue per discharge is being positively impacted by the temporary suspension of sequestration and by higher acuity patient mix resulting from the pandemic. We saw the acuity of our patients increase in the second quarter of 2020 and continued in the third quarter, and we expect this trend to continue in the fourth quarter.

As you can see on page 10 of the supplemental slides that accompanied our earnings release, our expenses did increase as a percent of revenues, primarily due to the COVID-19 pandemic. Our hospital teams have done a tremendous job managing our most significant cost, labor. For the third quarter of 2020, our employees per occupied bed, which we use as a metric to measure our efficiency, was 3.44 compared to 3.48 in the third quarter of 2019. This is evidence that our technology and real-time data combined with our clinical know-how makes us a best-in-class operator in any environment. We know how to effectively and efficiently manage our hospitals and can adjust our staffing levels to our volumes. We've also taken aggressive actions to obtain what we believe are adequate supplies of personal protective equipment even at the elevated utilization levels associated with the pandemic.

While some facilities in the post-acute space have faced significant challenges with COVID-19, our inpatient rehabilitation hospitals have been able to help recovering patients return to their independence. These patients, many of whom spent time on ventilators, have endured extended stays in acute care hospitals. They are extremely weak and require intense multi-disciplinary rehabilitation to regain both their strength and cognitive abilities. Since April, we have treated over 3,000 recovering COVID patients, returning 80% back to the communities following their rehabilitation.

In the fourth quarter of 2020, we expect limitations on elective procedures in certain markets to continue to impact volume growth, but we believe these volumes will return. It's a matter of when, not if. We remain confident in the long-term outlook for our hospitals, so much so that we've continued to expand our national footprint throughout this pandemic. We've opened three new hospitals thus far in 2020, and we expect to open another one in Toledo, Ohio in mid-November. In addition, by year end, we expect to have added approximately 120 beds to existing hospitals with 89 of those already added. For 2021, we've announced plans to build eight new hospitals. We've also announced eight new hospitals scheduled to open in 2022. And we're not done making [indiscernible] (00:09:29). All of this fully demonstrates our commitment and confidence in our future.

Let's move now to our home health and hospice segment. Our home health volumes recovered substantially in the third quarter of 2020. While same-store admissions were down 4.6% compared to the third quarter of 2019, they improved significantly from the second quarter of 2020 when we saw a 17.3% decrease in admissions. And we came out of the quarter stronger than we entered it with year-over-year same-store admissions growth of 2.2% for the month of September. We achieved this success even with our year-over-year admissions related to elective procedures down approximately 20%.

Additionally, continued facility access restrictions has negatively impacted the volume of patients admitted onto our service who reside in assisted or independent living facilities and these admissions down approximately 40% year-over-year. We also continue to experience COVID-related challenges in certain geographic markets, specifically in Texas where admissions were at 95% of our 2019 levels in the third quarter of 2020, mostly due to limited elective procedures. While admissions in Florida dipped to 91% of historic levels in August, they rebounded nicely in September to finish the quarter above 100% of Q3 2019 admissions.

Even in the face of restricted access to some of our historic referral sources and with limited elective procedures in many of our markets, we continue to perform at a high level. Cost controls remain strong in home health with our cost per visit down almost 4% in spite of COVID-related expenses associated with PPE and staff and quarantine.

Our most significant decline in volume has been in the physical therapy discipline due to the decline in elective procedures and being shut out from assisted living facilities. To adjust for this, in May, we made a shift in our compensation structure for therapists, lowering each therapist's base pay by 20% and in turn, lowering their productivity expectations per each pay period by 20%. This change allowed us to save costs and do so in a manner that did not result in any broad furloughs, layoffs or terminations. We plan to keep this compensation structure going forward as it allows us to better flex our therapy staffing and allows our therapists to earn additional compensation by exceeding their productivity levels.

Although the pandemic has made some collaboration efforts more difficult and necessarily virtual in nature, we believe there is a strong interest in partnering with Encompass Health home health and hospice segment among ACOs and Medicare Advantage payers seeking value-based payment arrangements. We have partnered with more than 100 Medicare Shared Savings Program ACOs around the country, adding nine new ACOs to this list in the third quarter of 2020. A recent analysis of 2019 claims data revealed that we grew our share of ACO beneficiaries by 16% in 2019 versus 2018, whereas the rest of the home health industry remained flat year-over-year.

Similarly, our continued efforts to enter value-based payment arrangements with Medicare Advantage payers yielded the addition of two new contracts in Q3, with more discussions ongoing and anticipated to result in additional contracts over the coming quarters. With the combination of industry-leading hospital readmission rates resulting in more healthy days in home for our patients, success in 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. And after several months of unusually slow M&A activity in the home care sector, we are encouraged that the pipeline of acquisition opportunities is rebuilding, particularly for hospice.

Despite the pandemic, we're continuing to find new and effective ways to provide care to our patients and support our clinicians in both business segments. Reducing readmissions remains a focus for us. As many of you know, our ReACT model focuses on preventing acute care transfers while patients are in our inpatient rehabilitation hospitals. This month, we rolled out our Readmissions Prevention Program (sic) [Readmission Prevention Program] (00:15:00) which uses information from more than 400,000 patients who have been through our inpatient rehabilitation hospitals or home health agencies to estimate a patient's risk of hospitalization after discharge. We use this score combined with social determinants of health and our clinical judgment to estimate and act on a patient's overall probability of being hospitalized and hopefully prevent a readmission from occurring.

In our overlapped markets, our hospital and home health teams are working together to ensure a smooth transition to the home and have established clinical protocols to help mitigate the need for both emergency care and hospitalization for high risk patients. This is another way we are using data from our electronic medical records from both segments to predict a potential decline in health status and act in a timely manner to prevent it. This is good for patients and payers.

While many uncertainties continue to exist, our visibility has improved and we have more information and experience in managing our operations during the pandemic. Therefore, we had issued guidance for the fourth quarter of 2020. You can see this guidance in our earnings release as well as on page 17 of the supplemental slides that accompanied the release. We expect to be in a position provide full year 2021 guidance and a longer-term outlook when we report our Q4 and full year 2020 earnings at the end of January.

While many uncertainties still exist, our company is well positioned to drive long-term growth. As I mentioned at the beginning of my comments, we have a proven track record of adapting to and working through challenges, including this pandemic. Our business fundamentals aren't changing. In fact, the pandemic has created an even stronger awareness of the high level of care we provide in our inpatient rehabilitation hospitals and the value of our home health and hospice service lines. And as the population ages, the demand for a high-quality care will increase. I believe our future is bright.

Before I end, I want to thank all of our employees who continue to make Encompass Health a leader in integrated healthcare. 2020 has been an unprecedented year. Our nation has been through a lot. And yet our employees have continued to care for our patients, striving for better outcomes compared to those of other care settings. I can't thank them enough and I know our patients are grateful for their efforts too.

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. Let me reiterate what Mark just said, we are very proud of our team's response to the ongoing pandemic and we're very pleased with the resiliency our organization has demonstrated. This is evident in the continued improvement of our financial results.

For Q3, our consolidated net revenues increased 1.1% over Q3 2019 to $1.174 billion. And our consolidated adjusted EBITDA for Q3 was essentially flat to the prior year period at approximately $230 million. Even in these challenging times, our business continues to generate strong cash flow. Our Q3 adjusted free cash flow of $124.1 million, increased 13.2% over Q3 2019, bringing our year-to-date adjusted free cash flow to approximately $367 million. Our strong and consistent cash flow supports our complementary strategies of investing in growth opportunities and making shareholder distributions.

Through the first three quarters of 2020, we have made approximately $159 million in growth investments and provided approximately $89 million in shareholder distributions. We continue to proactively manage our capital structure to ensure adequate liquidity and flexibility to navigate our business through any challenges and to capitalize on the attractive growth opportunities we see in all three of our service lines.

In late September, we again accessed the debt markets, raising $400 million in senior unsecured notes with a coupon of 4.625% maturing in 2031. This transaction settled in early October and thus is not reflected on our [indiscernible] (00:20:01) Q3 balance sheet. The proceeds from this offering will be used together with approximately $300 million of cash on hand to retire the balance of our 5.75% senior notes due in 2024, resulting in both lower interest expense and a longer duration of our debt capital. Our net leverage at the end of Q3 was 3.6 times and we finished the quarter with no amounts drawn on our $1 billion revolving credit facility.

Both of our business segments have continued on an upward trajectory following the [indiscernible] (00:20:39) in our volumes reached in mid-April. This has been accomplished in spite of the COVID case surges in some of our most important markets. Beginning with the IRF segment, total revenue increased 3.1% over Q3 2019 as inpatient growth of 3.8% was partially offset by a 25.3% reduction in outpatient and other. The decline in outpatient revenues stems from permanent unit closures in 2019 and the intermittent suspension of certain units in response to the pandemic in 2020. Q3 discharges declined 1.5%, with a 2.8% drop in same-store discharges, partially offset by new store contributions. Much of the same-store decline was attributable to our facilities in Florida and to a lesser extent, Texas where the effects of the pandemic had been high.

As can be seen on page 6 of the supplemental materials, our patient census increased throughout the quarter. We continue to see strong growth in our Medicare Advantage business with MA discharges increasing 40.6% in Q3. As Mark stated, we continue to experience higher patient acuity in Q3. The increase in average acuity together with the Medicare sequestration suspension were primarily responsible for our 5.4% increase in revenue per discharge. The higher acuity drove an increase in our average length of stay, which partially offsets this pricing benefit. Our revenue per patient day for Q3 increased 2% over the prior year.

IRF segment adjusted EBITDA for Q3 of $209.2 million, declined less than 1% from Q3 2019. Our hospitals continued to manage labor productivity and operating expenses very effectively during the quarter. These efforts notwithstanding the effects of the pandemic caused SWB in Q3 to increase 20 basis points as a percent of revenue over the prior year period and supplies to increase 80 basis points as a percent of revenue.

Home health and hospice segment revenue in Q3 declined 5.1% from the prior year period. Home health revenue decreased 6.5% based on the 3.3% decline in admissions and a 2.3% drop in revenue per episode. The decrease in revenue per episode is primarily attributable to the implementation of PDGM, the effects of which have been exacerbated by the pandemic. Home health revenue per episode in Q3 benefited from the suspension of the Medicare sequestration as well as the increase in admissions late in the quarter.

Our Q3 hospice revenue increased 1.6%. Hospice same-store admissions in Q3 were up 15.8% but patient days declined 2.1% due to a lower average length of stay resulting from a change in our patient mix. During Q3, the percentage of our referrals from institutional settings, which typically have a lower average length of stay, increased while the percentage of referrals from senior living facilities, which typically have a higher length of stay, decreased. This is due to access restrictions in many senior living facility referral sources owing to the pandemic.

Within home health, our continued focus on labor productivity combined with compensation structure changes implemented earlier this year drove a 270 basis point reduction in cost of services for Q3. Visits per episode declines from 17.3 in Q3 2019 to 16.4 in Q3 2020 and cost per visit declined to $75 from $78 in the prior year period. This effective cost management led to segment adjusted EBITDA in Q3 of $51.8 million, an increase of 2% over Q3 2019.

As Mark stated, we've issued guidance for Q4. The guidance and the key considerations on which it's based can be found on pages 17 and 18 of the supplemental materials. The Q4 guidance includes an adjusted EBITDA range of $225 million to $240 million as compared to $238.2 million achieved in Q4 2019. As noted on page 18, adjusted EBITDA in Q4 last year benefited from $9.5 million of items we do not expect to repeat this year.

And now, operator, we'll open the line for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And your first question comes from the line of Whit Mayo of UBS.

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

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

<Q – Whit Mayo – UBS Securities LLC>: Hey, thanks for all the color this morning. I wanted to start with just the home health volumes. If we adjust for the assisted living, the senior referral declines, what would the year-over-year volumes be, I mean, if we just isolate – I mean, the 40% decline just strikes me as very high and I get that that COVID makes forecasting difficult. But I'm curious maybe to hear from April any experiences that you could share in markets outside of Florida or Texas that might be trending more favorably. And does it make you more negative or optimistic on the outlook for volumes going forward?

<A – April Anthony – Encompass Health Corp.>: Yeah, Whit. So I think that the AL/IL community impact has been pretty significant and pretty consistent across the country. We haven't really had certain regions that have said, oh, just come in, openly welcome in. It's been pretty much a lockdown consistently across the country and as things begin to kind of ease up in the August, late July timeframe, we started to get a little bit greater access, but now as we kind of move a little bit into a period of spike, it definitely feels like we're again sort of seeing – particularly in certain markets in the Northeast, again, beginning to see some lockdowns and they're saying we'll let your nurse in but not your therapist, we'll let your nurse in in hospice, but we won't let your chaplains or social workers in. And so, it's just been a little bit of a mixed bag market-by-market.

And I think that market is probably one that we think is going to continue to be challenging for a bit. What we've done, I think, pretty well though is create some mitigating opportunities by really going out and using that [ph] disruption to causes (00:27:51) to look for some new sources of revenue. We've got a much increased flow from alternative surgery centers that are starting to pick up some of these electives. And in the area of electives, we're seeing a lot more positive movement pretty consistently from month-by-month, July, August, September, even into the first three weeks of October, where it looks like our decline in electives is down if you compare it to a pre-COVID level, down only about 12% from where it was in the January-February timeframe. So we're pretty encouraged about the trajectory that we're seeing everywhere other than AL/IL, which just continue to seem to be a little bit of a roller coaster but still consistently on the downswing.

<Q – Whit Mayo – UBS Securities LLC>: So just to be clear, if we could exclude the assisted living referrals, is there a number to think about in terms of how the business would be declining or increasing right now?

<A – April Anthony – Encompass Health Corp.>: I don't have that – I don't have it calculated that way right off the top of my head, but we can certainly look at that detailed information and try to get back to you with something.

<Q – Whit Mayo – UBS Securities LLC>: Okay. And just one last one just for both businesses, the monthly ADC disclosures are helpful. Is there any spot number, Doug, to kind of look at for October at this point, just to get a sense of how we may be trending versus what appears to be a better September exit rate?

<A – Doug Coltharp – Encompass Health Corp.>: [ph] A trend line (00:29:19) is good.

<Q – Whit Mayo – UBS Securities LLC>: Okay. I'll take that. Thanks, guys.

<A – Mark Tarr – Encompass Health Corp.>: All right. Thanks, Whit.

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

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

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

<Q – Joanna Gajuk – BofA Securities, Inc.>: Good morning. Actually, this is Joanna Gajuk filling in for Kevin today. So I appreciate...

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

<Q – Joanna Gajuk – BofA Securities, Inc.>: ...taking the question here. So thank you very for summation of the volume trends in home health. Can we talk about – a little bit about pricing trends in home health? So I guess, it wasn't a little bit. It was down like 2% after being down 1% in Q2 year-over-year. So can you just flag any items there? Is there any change in mix or anything around PDGM, which probably is hard to parse out but any kind of color you can provide on that would be great?

<A – April Anthony – Encompass Health Corp.>: Sure. Well, obviously, the revenue per episode is affected pretty significantly by those elective – elective procedures tend to be one of the – the joint replacements in particular tend to be the one of the higher revenue sources even under PDGM, although PDGM, that category is lower than it was under PPS back in 2019.

So when we see that decline in elective and we compare 2019, 2020, you have to kind of look at a combination of two factors. One, PGM would have made those procedures with less than they had been in the prior year, but secondarily we've also in 2020 got a little [ph] unfortunate with those (00:30:50), but still this is still higher than others. And so it's kind of a combination on the rate side of both the PGM implications and the proportional decrease that we see in elective procedures which are relatively high revenue sources. Does that make sense?

<Q – Joanna Gajuk – BofA Securities, Inc.>: Yeah. That does make sense. And if I can just follow-up on the commentary now on the other side – on the other segment on the inpatient rehab, in terms of obviously very impressive plans – new development plans for the IRF segment. So is that fair to say that you're not seeing much of a slowdown there in terms of any of these COVID cases spiking in some of these markets in terms of actually completing these projects on time? Thank you.

<A – Mark Tarr – Encompass Health Corp.>: So we do not. We think the basic fundamentals on the IRF side of the business continued to be strong both near-term and long-term. We see COVID as just a near-term challenge for us that we will get through as a matter of fact. If anything, COVID has given us an opportunity in the marketplaces to show the caliber of the high level of acuity care we can provide to our patients. So we don't see any impact with COVID on our development efforts.

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

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

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

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

<Q – Matt Larew – William Blair & Co. LLC>: Hey, good morning. Doug, thanks for all the detail on the guidance for Q4. I did want to ask about just a little bit on the pricing side. Obviously, the last couple of quarters have been very strong for IRF. And now moving into IRF calendar year that starts in October, you get a nice pricing boost. So could you maybe help us understand or quantify to some extent what acuity and sequestration benefit were in the quarter, maybe that can give us a window on to what pricing growth might look like in the fourth quarter for IRF?

<A – Doug Coltharp – Encompass Health Corp.>: Yes. So the sequestration is pretty straightforward, right, that's the 2% that you see. With regard to pricing, it's a little difficult to separate out the amount that is specifically related to patient acuity that may be driven by COVID activities. You've got two things that are going on with regard to acuity that are COVID related and Mark reviewed these in his comments.

The first is, you've got a portion of the patients that are coming in that are recovering from COVID and there is an extra comorbidity payment that comes along with those payments or with those patients that will boost the revenue per episode. But you've also got the change in the patient mix because we're seeing relatively the same number of stroke in neurological patients, but we've dropped out those lower acuity or repeat patients that Mark talked about. We expect those trends are likely to continue in the fourth quarter. Those had about – if you combine those and the other thing I wanted to throw into the mix is there's an element of this that is still the adoption of Section GG and it's difficult to separate out the impact of patient mix from COVID from GG. But together, we think those were responsible for about 190 basis points of the lift in revenue per episode for Q3.

<A – Mark Tarr – Encompass Health Corp.>: Matt, just a little bit more color to back what Doug is talking about. If you think about just from a Case Mix Index, we ran for a number of years right at the 1.36, 1.37 Case Mix Index. Starting this year in Q2 and carried over into Q3, we ran a 1.44 and a 1.42 Case Mix Index. So it's just indicative of the acuity that we're seeing that's coming out of the acute care hospitals. Remember, 90% of our admissions that come into our IRFs come directly from acute care hospitals. So these patients are just sicker. And whether they are specific to COVID or not, we're just seeing a higher acuity across the board.

<Q – Matt Larew – William Blair & Co. LLC>: Yeah. Thanks, Mark. That's what I was looking for. And then maybe just thinking about 2021, you mentioned you will give guidance early next year. But I think about half the locations in terms of IRFs coming on board next year are in Texas and Florida. Any reason at this point to think that the sort of on ramp of those facilities might be any slower than I think you said [ph] you're going to take (00:35:38) long-term plans and my takeaway from this call is that it sounds like nothing about your long-term outlook has changed at least qualitatively.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. I think with regard to the ramp up of the new facilities that are coming onboard, most of those are scheduled to come on board in Q3 of next year. We've got some that are opening late in Q2 and I think it's either our expectation or our hope or the combination of the two that we're going to be largely on the other side of the effects of the pandemic by that time. So we're not really anticipating anything different with regard to the ramp up there. And absolutely, nothing has changed regarding our enthusiasm and commitment to long-term growth prospects of the businesses that we're in. And so we will continue on the course that we have started down with regard to the development of an increased de novo pipeline in the IRF segment.

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

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

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

<A – Doug Coltharp – Encompass Health Corp.>: Hey, Brian.

<Q – Brian Tanquilut – Jefferies LLC>: Hey, good morning, guys. Good morning. Just to follow up on Matt's question, I guess, for both of you guys, if we're thinking about the growth algorithm, right, I mean, without going into guidance for next year, if I'm using kind of like the Q4 guidance as a baseline, is it right to assume that you should be able to grow on top of that and what would be the drivers of that growth as I think about 2021?

<A – Doug Coltharp – Encompass Health Corp.>: I think the continuing effects of the pandemic aside because again it's our anticipation that you're going to have those at a pretty significant level in Q1 and probably lingering through much of Q2, we've put some capacity in place over the course of 2019 and 2020 that provides room for organic growth. I mean, if you look at the bed additions we have made in 2019 and then another 120 bed additions coming on board in 2020, those are vehicles for same-store growth in 2021. And then we certainly would expect a recovery particularly in some of these harder hit markets as COVID works its way through the system. So we think there are good prospects for growth, particularly the back half of 2021.

<Q – Brian Tanquilut – Jefferies LLC>: Got it. And then, I guess, the question I have for April. How are you thinking about your PDGM mitigation efforts, right? Because I think the guidance for Q4 calls for a 2% to 3% headwind from PDGM. And I know when we started the year, we were thinking about a gradual mitigation to where we get to zero midyear to exit of 2020. So is there anything that has changed? Or just curious, how you're thinking about that and also sort of the sustainability of that $75 cost per visit. I mean, I know you changed your comp structure, is that the right number to be thinking about going forward?

<A – April Anthony – Encompass Health Corp.>: Yeah. So I think as it relates to PDGM mitigation, I'm pretty proud of what we've been able to do in spite of the challenges to see the revenue down 5% but the earnings up 2% really speak to the mitigation that we were able to do, whether be volume based or rate based in the quarter. Now, obviously, some of the things that we had planned to do from PDGM perspective that's proven to be exponentially difficult in a pandemic environment. For example, we were going to try to realize some of that assumed behavior change as it [indiscernible] (00:39:15) that has been actually going the other way on us during the pandemic.

So there've been a number of our strategies that we would have said were in place in January that have gotten to be particularly difficult in a COVID environment, but we've been able to do other things. And as you know, one of the significant things has been the comp adjustment that's resulted in improved cost per visit. I do think that within the therapy discipline, we're going to continue to see those savings coming through as we go forward as we maintain that comp plan. However, I think we're going to see some mitigation of that savings as it relates to the nursing discipline.

As you've likely heard, nursing staffing across the country is particularly challenged. We're seeing compensation rates go up. And so we would expect that we'll see some increases in cost per visit in the nursing discipline that may mitigate some of the savings we've picked up on the therapy side of the equation. So probably a little bit of cost climb as we move into 2021 and throughout the year.

<Q – Brian Tanquilut – Jefferies LLC>: All right. Got it. Thank you.

Operator: And your next question comes from the line of Matthew Gillmor, Baird.

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

<A – Mark Tarr – Encompass Health Corp.>: Hey, Matt. Hello, Matt?

Operator: Matt, your line is open, if your phone is on mute.

<Q – Matt Gillmor – Robert W. Baird & Co., Inc.>: Hey, I'm sorry. I was muted. Good morning, everyone.

[indiscernible] (00:40:38)

<Q – Matt Gillmor – Robert W. Baird & Co., Inc.>: I'm hoping to ask about the fourth quarter guidance. It's a relatively wide range on EBITDA for you all, which is certainly understandable given the pandemic. I was hoping either Doug or Mark can maybe give us some sense for what you're assuming from a volume standpoint within the guide, so we could just understand how you're approaching it?

<A – Doug Coltharp – Encompass Health Corp.>: That's kind of a wild card and the reason that we have a broader range is the thing that is most difficult to predict in this environment is the impact on volumes of any surging case experiences with related to COVID. So the top end of our range assumes that we continue to see the type of gradual volume recovery in both the business segments that we've experienced through Q2 and Q3 and the bottom end of the range assumes that there's some pullback.

<Q – Matt Gillmor – Robert W. Baird & Co., Inc.>: Okay. Fair enough.

<A – Mark Tarr – Encompass Health Corp.>: And as we said, we certainly came out of Q3 stronger than we went into it and we're very pleased with the progress made in September and that momentum was carried over into October. So like Doug said, I mean, the wildcard is the assumptions or the surge around COVID that we are certainly pleased with the momentum that we made through Q3 and have carried over into Q4.

<A – Doug Coltharp – Encompass Health Corp.>: The other thing that injects some variability into the EBITDA range for Q4, Matt, relates to the self-insurance accruals. So as we indicated on the guidance considerations, we had $7 million in positive accrual adjustments in Q4 of 2019. And this year is a little bit difficult to predict. And I recall in the second quarter, we had a nice lift from lower claims activity in both group medical and workers' comp. We had expected that we would see claims activity under both of those programs pick up in Q3 for different reasons.

One is, as the medical system began to open up and there was some deferred demand, we expected our employees and their families who were beneficiaries into the group medical plan to start to go out and have more maintenance services, including some elective surgeries. And we did see that, not fully back but we did see it come back pretty substantially. And we also knew that we were seeing a larger number of workers' comp claims related to people who acquired or employees who acquired COVID in one of our facilities. So that was work related.

Well, what we know is that even though there is a higher number of those claims, the payout on those claims is substantially lower because they tend not to be severe cases and they tend to be short-term in nature. So we're not sure what to think about those claims activities as we move into Q4 and that against the favorable accrual adjustments that we had in 2019 creates a little bit more variability and that was embedded in our thinking with regard to a broader range for Q4 than we normally have with regard to the EBITDA.

<Q – Matt Gillmor – Robert W. Baird & Co., Inc.>: Okay. And then one follow-up on the Medicare Advantage mix in the IRF segment. I think you said MA volumes were up 40% and certainly that's a big acceleration from where that trend was prior to COVID. And I think maybe in the past, you've said that some of these plans were waiving pre-authorization requirements. Just hoping to get some insight into the sustainability of that trend, if you can.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. So what was driving that higher MA volume and remember, we were up 66% in Q2, so that came down a little bit to 40% but remains very high in Q3 was both an increase in referrals and an increase in admits based on a higher conversion rate. So, for Q3, our referrals were up 23% over Q3 last year and admits were up 38% based on a 170 basis point increase in the conversion rate. That was done largely without the pre-authorization waivers in place for most markets during Q3. And it's our expectation that the pre-authorization requirements that are in place right now because they've essentially all been reinstated are going to stay with us into Q4.

We expect based on these, what we saw with regard to the monthly trend throughout Q3, we expect to see a normalization in our payer mix in Q4, which means the MA growth rate is going to remain high, but it's going to come down. And if I were to just give you an estimate right now, I would expect to see MA discharge volume growth in Q4 probably closer to the 15% to 20% range. So slightly elevated from maybe the level that we averaged in 2018 to 2019, but still growing at a good clip and probably something that we would deem to be in the sustainable range at least in the 2021.

<Q – Matt Gillmor – Robert W. Baird & Co., Inc.>: Okay. Thanks a lot.

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

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

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

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Hey, how are you, guys? First of all, I just – you have a slide 20 in your deck that talks about the acquisitions and the de novos. And I'm just curious because I think you still have in there $50 million to $100 million in M&A in 2020 and maybe I've missed it, but I think that's new and – but is that – I think there hasn't been any so far. So is that then you see something in the fourth quarter coming and is there any update? You had $97 million on de novos year-to-date, and I think at one point you had assumed $180 million to $190 million up, is that just the COVID process has slowed it down or is there going to be a bolus of them coming into the fourth quarter on de novos as well?

<A – Doug Coltharp – Encompass Health Corp.>: Yes. So I'll start with the second part first, that is there's been a little bit of an impact on pacing related to COVID this year, but we would still expect that based on what we're doing in the fourth quarter to see the range for that de novo number still fall into $180 million to $190 million in 2020, which means we're going to be pretty busy in Q4 and we are pretty busy on numerous projects.

Then on home health, as Mark mentioned in his comments, we have seen a pickup in the acquisition pipeline. There's some activity that's out there right now. It's more heavily oriented toward hospice than it is home health. But this $50 million to $100 million reflects perhaps the degree of optimism that we're going to be able to get a deal or two done in the fourth quarter.

<Q – A.J. Rice – Credit Suisse Securities (USA) LLC>: Okay. That's good. And maybe my follow-up question would be there have been some studies that have come out and there have been some proposals from individual legislators in Congress about potentially looking at rolling back the behavioral adjustment that was in the original PDGM legislation or regulations rather. And I don't know – I'd be interested to know in your discussions whether you're seeing any momentum behind that. Do you think as we come out of this election season, the prospects have improved that maybe we'll see some favorable developments on that front?

<A – April Anthony – Encompass Health Corp.>: I do think that we're having some big conversations and that they're very data-driven conversations in Washington. What I would say, I don't expect that it will affect the 2021 rate. We expect that rate proposal to come out perhaps as soon as Friday, but certainly within the next 10 to 12 days. And so I don't think we're going to see a recognition of the behavioral change assumptions being [ph] plotted (00:48:53) for this coming year's rates. But I do think that we're in a very good position to have the 2022 rate being adjusted for that.

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

<A – April Anthony – Encompass Health Corp.>: And the data [ph] that's plotted by Dobson and DaVanzo (00:49:07) and others is very strongly in support of the fact that the assumptions were not well founded and have not proven to be accurate. Even if you try to COVID adjust them, I think their data would suggest they were way off the mark.

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

Operator: And your next question comes from the line of Ann Hynes of Mizuho Securities.

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

<A – Doug Coltharp – Encompass Health Corp.>: Hey, Ann.

<Q – Ann Hynes – Mizuho Securities USA LLC>: Hi. Good morning. So my first question has to do about with the eight new hospitals opening in 2021. From even a contribution perspective, should we view that class as being a negative EBITDA drag or positive? And can you remind us just with the de novos, how we should view the EBITDA contribution and margin expansion over the first two years after you open the de novo?

<A – Doug Coltharp – Encompass Health Corp.>: Yeah, Ann, so I would expect as a class that they are going to be EBITDA negative in 2021. You know from information that we've historically published that our preopening expenses associated with a hospital, which typically begin about six months in advance of the opening date, run at about $1 million per facility. And we don't expect that would be any different with regard to this class.

And then with regard to the ramp up rate, we refer you to the slide that we've included for a long period of time, the investor reference book which shows our historical activity in terms of hospitals achieving four-wall positive EBITDA. And depending on the market, depending on other circumstances related to the market, the earliest of that typically happens is about nine months. And usually, it would be odd if we didn't hit kind of a four-wall EBITDA positive contribution within 18 to 20 months. So, it's somewhere in that range.

<Q – Ann Hynes – Mizuho Securities USA LLC>: All right. Thanks. And then my second question. Obviously, you have not given 2021 guidance, but can you maybe address some other key headwinds and tailwinds that we haven't discussed yet on the call and in particular, can you address ongoing PPE cost? Thanks.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah, just – I know everybody is anxious to start thinking about 2021. We are – there is nobody on this call who is not ready to be done with 2020 and get into next year. So we certainly share that view. Probably like a lot of other companies and maybe even the business you're in, normally, we would be very late into the budgeting process both in terms of the formation of our operating budgets and the capital budgets by this time. And we've essentially deferred the whole budgeting timeline by about two months because we felt like depending on the course of the pandemic, we could find ourselves in a position where we had done the budget base, which is a lot of work, based on one set of assumptions only to find that as we entered the new year, there was a new set of assumptions. I just want to throw that out there as a caveat as to why we're not giving more color regarding 2021 during this call.

With regard to the expenses, we think we've got a pretty good handle on expenses right now. So if we think about the pandemic continuing into the first half of 2021, kind of run rate that we're experiencing right now is probably a pretty good proxy for what we'll see in the first half. And then as we move beyond the pandemic in the second half, we would expect to be able to realize some efficiencies with regard to both labor and with regard to supplies cost.

<A – Doug Coltharp – Encompass Health Corp.>: Ann, we put – you might want to check out slide 25 in our earnings slide book. We try to expand on the PPE cost, and Ann, I'd just say that we're in a much better position now than we were even six or eight months ago relative to PPE and our team's done a great job going out and finding secondary suppliers to help meet our demand needs.

<Q – Ann Hynes – Mizuho Securities USA LLC>: Yes. No, I did see that slide. I was just wondering if you think it would be a headwind for all of 2021 and even going into 2022, or do you think this extra cost is more transitory in nature?

<A – Doug Coltharp – Encompass Health Corp.>: I think the bulk of it is probably more transitory although as we've said previously, my guess is that none of us in the healthcare world are going back to pre-COVID normal that there's going to be some heightened use of PPE that stays with us on a go-forward basis. And I think in this organization, we believe that's absolutely proven.

<Q – Ann Hynes – Mizuho Securities USA LLC>: All right. Thanks.

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

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

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Hey, good morning, guys. This is Pito Chickering here. A couple of quick questions for April. There are some moving parts about what you're talking about on the cost per visit as it relates to nursing disciplines going forward. Conceptually, should we use the $75 per visit as a starting point and grow it 3% to 5% over the next 12 months, or can you help just conceptualize how that works?

<A – April Anthony – Encompass Health Corp.>: We haven't, as Doug mentioned, really wrapped up our budgeting process and our planning for next year, and I think we feel like there is some significant challenges on the staffing side but there are things that are going to drive costs up. I can't say that we're seeing that everywhere and broadly yet, but certainly in certain markets, we're seeing some of that.

So I think it's reasonable to assume that it will be a little bit of a plain up over the course of 2022. As pandemic goes away quicker, we may see some nurses that had previously retired return to the market and things could sort of like ease up a little bit, but I think it's probably reasonable to assume just a little bit of a steady plain of increase in the nursing discipline throughout the course of 2021.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Okay. Great. And then visits per episode were relatively unchanged in third quarter versus first quarter. I would have assumed that with the Metalogix roll out, we would have seen some reductions in those visits. How should we be thinking about sort of that the visits per episode declining over the next sort of 12 months or so?

<A – April Anthony – Encompass Health Corp.>: Yeah. As we mentioned in prior calls, our deployment of the Metalogix tools got a little bit delayed as a result of the pandemic. I think we didn't get it fully deployed until June-ish timeframe. And then it just takes a little while to change practice and get people in especially when your deployment was a virtual deployment versus a hands-on face-to-face training approach. I think we have not really begun to scratch the surface fully of the opportunity with Metalogix and that we will continue to see improvement quarter-over-quarter as we get that fully baked into our processes, in our thinking and our approach.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: All right. Great. And then last quick one here for you. What percent of your business is tied to assisted living? I apologize if I missed that. And looking at 2018, what percent of your growth came from that type of business? Thanks so much.

<A – April Anthony – Encompass Health Corp.>: I don't have a specific figure right in front of me right this second. But AL/IL communities have been around 20% – 15% to 20% in the past. And that category is one that's kind of off in the 20% to 25% range in the COVID world for the reasons we've touched earlier.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: Okay. But ballpark is, like, assisted living is just like a 5% of your exposure, is this like 25%, is this – [ph] just some color (00:56:37) would be helpful.

<A – April Anthony – Encompass Health Corp.>: I think [indiscernible] (00:56:39) 15% to 20% of our total patient volume resides in AL/IL communities.

<Q – Pito Chickering – Deutsche Bank Securities, Inc.>: All right. Great. Thanks so much, guys. Nice quarter.

Operator: And your next question comes from the line of Frank Morgan of RBC Capital.

<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. Hey, I wanted to go back to, I guess, tail end of the A.J. question about the likely M&A activity. You certainly mentioned in your opening remarks you expected a pick up on the hospice side. And I'm curious I would've thought by now that maybe you would see more on the home health care side, but just curious on your thoughts about why do you think you're seeing it more on the hospice side versus the home health care side.

And then secondly, I appreciate the color to Whit's question about sort of the ending point for census. A lot of our other provider calls have indicated that September ended on a strong note, but a lot of them are talking about they are starting to see a COVID surge again. So just any color there, I would appreciate that as well. Thanks.

<A – Doug Coltharp – Encompass Health Corp.>: So I think I'll hit on the first part and then I'll turn it over to April. Hospice has generally speaking been significantly less impacted by the events of 2020 than home health. So you've got a better run rate and it's easier to engage in price discovery for a buyer and a seller. And the two things that we would point to is, one, hospice was not subject to a payment system form like PDGM. And then hospice volumes were less impacted at any point in time by COVID.

And so when you layer on everything that's going on with regard to COVID on top of PDGM and with the pandemic having come into play before providers had an opportunity to establish a new base rate, a new baseline, I should say under PDGM, it just makes getting to a run rate EBITDA on which to have meaningful discussions regarding a potential transaction very difficult and those same limitations don't exist in hospice.

And for both businesses, I think that there is an awareness that there is very favorable growth opportunities and that's reflected in the multiples. So if you are an owner of one of those businesses and have been thinking about transitioning out, right now is a pretty good time to do so from a hospice perspective.

<A – Mark Tarr – Encompass Health Corp.>: Frank, I'll ask both April and Barb Jacobsmeyer to weigh in on what they're seeing in the current marketplace relative just to COVID.

<A – April Anthony – Encompass Health Corp.>: Yeah. Well – and so, I would also say on the home health side, I think we came into this year expecting PDGM to really disrupt home health providers and for that to create a wave of opportunity and acquisition. And with the PPP loans, the advance payments and then the CARES Act funds, a lot of those smaller midsized agencies that we thought would feel a significant level of disruption did not feel that disruption in spite of COVID.

So the combination of the complexity Doug mentioned and then all this secondary support that is not going to continue long-term, we think it's just really kind of kicked the can down the road a year for some of that home health disruption. So we still expect that we'll begin to see some of that tick back in 2022, particularly if some of those advance payments have to start being repaid here pretty shortly.

<A – Barb Jacobsmeyer – Encompass Health Corp.>: And I would say on the census side for the IRF side, I mean, October is certainly looking similar to the year-over-year that we've seen in September. But what I would say is what we've experienced really throughout COVID has been market-by-market challenges and those certainly are continuing. So we see a decrease in one market and then it pops up in another market. So that has not changed. We're continuing to see that affect us on a pretty regular basis.

<Q – Frank Morgan – RBC Capital Markets LLC>: And maybe, April, could address that same question. Thanks.

<A – April Anthony – Encompass Health Corp.>: Yeah. Sorry, I overlooked that part of the question. So, yeah, I think like Barb, we definitely are seeing sort of ebbs and flows by market. I think our biggest challenge has really been that about 37% of our total admission volume comes from two states, Texas and Florida, both those states being hit pretty hard with the first wave and the second wave. And so we're encouraged in both states that we're seeing progress from the third quarter really even into the first three weeks of October.

And so we think we have learned to create some new referral sources. As I mentioned earlier, we're looking for ways to mitigate losses that we're experiencing from lack of electives as well as from the AL/IL impact. And so I feel encouraged by what we're doing and think that that would suggest that when we do start to see a return of norm in those two states and particularly with electives and AL/IL, we've got a sustainable trend to maintain new sources while adding back some of our old sources.

So I think we're going to continue to see noise from the COVID situation probably for the next six months. But we're working hard to create new avenues for growth and feel pretty positive about the trajectory that we're on.

<A – Mark Tarr – Encompass Health Corp.>: Frank, I certainly would never want to characterize it as routine. But our staff and I said in my opening comments, our teams have just done a tremendous job in, A, learning how to treat COVID patients, learning how to take the mitigating efforts they need to whether it's in a clinical setting or sales and marketing setting. I think that we have really set ourselves apart from our competitors in the marketplace with our willingness to take COVID patients into our service lines and then also the outcomes that we've achieved with them.

So I think it's given us a chance to really endear ourselves even more to referral sources and we talked about MA plans earlier. I think this has given us a chance to show MA plans, the value proposition that we have through our home health and IRF hospitals. So, overall, they have just done a tremendous job mitigating the impacts.

<Q – Frank Morgan – RBC Capital Markets LLC>: Thank you.

Operator: And your next question comes from the line of Sarah James of Piper Sandler.

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

<Q – Sarah James – Piper Sandler & Co.>: Thank you. Good morning. And I'm going to follow on on that kind of chain of thought for M&A here. So understanding PDGM disrupted, what's available and maybe stimulus money is elongating things as well, but when do you expect the home health market to get back to normal as far as the opportunity of what's out there for M&A and to the degree that you're leaning a little bit more into de novo, can you just remind us what the breakeven timeline is or ROI differences are for you on de novo versus M&A?

<A – April Anthony – Encompass Health Corp.>: On home health, I would say that we've probably got another, again, six months before we start to see home health really start to get interesting again. Again, it's going to get a burn through the CARES Act funds get back into your repayment requirements on advance payments, if those occurred. So I would think that home health is going to remain a little bit quiet all the way probably into the second quarter of next year.

Hospice, however, because as Doug mentioned, the multiples on that have been very nice and the marketplace, there've been some big announcements recently of high multiple transactions and the disruption has been far less, I think we'll continue to see a lot of frothiness in the hospice world from an acquisition perspective and would anticipate that over the next six months that will be where most of our M&A efforts are pointed.

<A – Doug Coltharp – Encompass Health Corp.>: So with regard to your questions on the IRF side and the comparison of the returns, Sarah, as we mentioned previously with regard to the breakeven point or the ramp up on in IRF, they typically achieve a four-wall positive EBITDA at the earliest between six and nine months and then probably on average closer to 18 to 20 months, that's based on our historic activity.

With regard to a return comparison, just a couple of data points to have out there. You could probably ballpark our weighted average cost of capital at somewhere depending on how you want to view the current market conditions, call it, 8%. So we're certainly looking to make sure that the returns that we're estimating from any of the investments we make in growth opportunities are going to land north of that, so that we're creating wealth. We intend to use a 13% IRR target for investments that we make. We've got a very good track record with regard to our de novos meeting or exceeding that target.

What you are seeing in home health and hospice is acquisition multiples push up. And as acquisition multiples push up, it becomes more difficult to receive outsized returns. So we're being very disciplined, as we always have been, with regard to that kind of activity. But if you get to a point where you're paying between 12 and 15 times on a business that isn't significantly impaired in terms of its current level of margin performance or doesn't have outsized organic growth opportunities, then your returns are going to be closer to that weighted average cost of capital than they are going to be to that 13%.

<Q – Sarah James – Piper Sandler & Co.>: Got it. That's helpful. Thank you.

Operator: And your final 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 acuity trends in your rehab centers. Even though acuity remains elevated on a sequential basis, both your revenue per discharge and length of stay decreased, which suggests moderating acuity. So I just wanted to get more clarity on why those numbers are moving lower if you are seeing intensifying acuity in your centers. Thanks.

<A – Doug Coltharp – Encompass Health Corp.>: Yeah. I think the – I'm checking my own numbers here, but I believe that sequentially the acuity and the length of stay actually increased. Our acuity in Q2 was 1.49, acuity in Q3 was 1.52 and with regard to the length of stay, I think we were also up...

<A – Mark Tarr – Encompass Health Corp.>: Almost half a day, I believe. [indiscernible] (01:07:05).

<A – Doug Coltharp – Encompass Health Corp.>: ...we were up, I've got it here in someplace, give me just a second. We were at 13 even, I believe, in Q3. We just put our fingers on the Q2 number.

<A – Mark Tarr – Encompass Health Corp.>: [indiscernible] (01:07:25)

<A – April Anthony – Encompass Health Corp.>: That's right.

<A – Doug Coltharp – Encompass Health Corp.>: We'll get that for you in just a moment. But I think – oh, here we go. The acuity for – and this is not sequential, but acuity for Q3 2020 was 13.2. It was 12.9 in Q3 of 2019. And I think it was about 12.9 in Q2.

<A – April Anthony – Encompass Health Corp.>: Length of stay.

<A – Mark Tarr – Encompass Health Corp.>: Length of stay.

<A – Doug Coltharp – Encompass Health Corp.>: Length of stay, excuse me.

<Q – Andrew Mok – Barclays Capital, Inc.>: Got it. Okay.

<A – Doug Coltharp – Encompass Health Corp.>: Those trend lines would be consistent to what you're seeing reflected in the pricing.

<A – Mark Tarr – Encompass Health Corp.>: Does that give you what you needed on the question?

<Q – Andrew Mok – Barclays Capital, Inc.>: I see the length of stay at 13.2 in Q2 and then down to 13 in Q3. So I was just more so looking for color on why that was moving lower, but if you are seeing intensifying acuity or any reversal of those trends, would love to hear more color on that.

<A – Doug Coltharp – Encompass Health Corp.>: No, we're not at this point.

<A – Mark Tarr – Encompass Health Corp.>: Only other factors that we saw early on in Q2 relative to our length of stay and it went over into Q3 too is just the ability to discharge patients from our hospitals to other post-acute settings was delayed in terms of their willingness to accept patients that had been treated for COVID. So that played a role in the extended length of stay in our hospitals.

<A – Barb Jacobsmeyer – Encompass Health Corp.>: I think what's also important to note is that and I think we talked about this earlier about the patient mix. So our other orthopedic conditions as a percentage of our patients went actually down 180 basis points quarter three of 2020 over quarter three of 2019. That does impact our CMI and our length of stay because then the patients in-house are much more acute. So if we do see the elective surgeries come back online for these patients that have a lot of comorbidities and start seeing that come back to our hospitals that could impact that CMI and that length of stay.

<A – Doug Coltharp – Encompass Health Corp.>: And so Andrew, to your point, you're right, sequentially, we were at 13.2 in Q2 and 13 in Q3 as compared to last year Q2 of 2019 was 12.5. So a delta of 0.7 and Q3 of 2019 was 0.4 – it was 12.6. So it was a delta of 0.4. So the specific length of stay against the higher CMI would have had less of an offsetting impact on the pricing – on how much of the pricing lift benefited us at the margin perspective, but both of those levels on a year-over-year basis are reflective of the higher acuity of the patients.

<Q – Andrew Mok – Barclays Capital, Inc.>: Got it. That's helpful. Thank you.

Operator: And I'll turn the call back over to Ms. Carlisle.

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

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

Operator: And thank you for participating. You may now disconnect at this time.