

Event Type: Q3 2021 Earnings Call

Date: 2021-11-11

Company: **Medical Facilities Corp.**

Ticker: DR.CA

COMPANY PARTICIPANTS

Robert Horrar - Medical Facilities Corp., President, Chief Executive Officer & Director

David N. T. Watson - Medical Facilities Corp., Chief Financial Officer

OTHER PARTICIPANTS

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, please stand by. Good morning, everyone. Welcome to the Medical Facilities Corporation's 2021 Third Quarter Results Conference Call. After the management's remarks, this call will include a question-and-answer session whereby qualified equity analysts will be permitted to ask questions.

Before turning the call over to management, listeners are reminded that certain statements made today – in today's call, including responses to questions, may contain forward-looking statements within the meaning of the Safe Harbor provisions of Canadian Provincial Securities laws. Forward-looking statements involve risks and uncertainties and undue reliance should not be placed on such statements. Certain material factors or assumptions are applied in making forward-looking statements, and actual results may differ materially from those expressed or implied in such statements.

For information about factors that may cause actual results to differ materially from expectations and about material factors or assumptions applied in making forward-looking statements, please consult the MD&A for this quarter in the Risk Factors section of the annual information form and Medical Facilities' other filings with Canadian Securities Regulators. Medical Facilities does not undertake to update any forward-looking statements. Such statements speak only as of the date made.

Please note that today's call is being broadcast live over the Internet and the webcast will be available for replay beginning approximately one hour of the completion of the call. Details on how to access the webcast replay are available in the morning's news release announcing the company's financial results.

I would now like to turn the meeting over to Rob Horrar, President and CEO of Medical Facilities. Please go ahead, Mr. Horrar.

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Robert Horrar

Thank you, operator. Good morning and welcome to our third quarter earnings call. Joining me today is David Watson, our Chief Financial Officer. Earlier this morning, we released our third quarter results. Our news release, financial statements, and MD&A may be accessed through our website at www.medicalfacilitiescorp.ca and have also been filed with SEDAR today.

We were pleased with our continued solid financial results over the first nine months of 2021, despite a surge in COVID-19 cases across the United States in the third quarter, our revenues were in line with Q3 of last year when we experienced a strong rebound in surgical case volumes following the first wave of the pandemic. Our volumes this quarter were short of 2019. We're also impacted by the loosening of travel restrictions and the corresponding increase in provider vacations. Regardless, for the first nine months of 2021, our facility service revenue is up 12.2%, income from operations is up 12.3% and our EBITDA is up 7.3%. We've improved our financial flexibility during this time and reduced our debt significantly over the past two years. As a result of this and our continued strong cash flow performance, we were pleased this morning to announce a 15% increase to our quarterly dividend commencing with the fourth quarter dividend. Dividend is an important part of our commitment to maximizing total shareholder return. Additionally, the board of directors has approved implementing a normal course issuer bid for up to 5% of the corporation's issued and outstanding common shares, subject to the approval of the TSX.

The fourth quarter is typically our busiest time of the year, and we remain cautiously optimistic about our outlook. We are monitoring volume recovery closely and encouraged by the recent downward trend in new COVID cases across much of the United States.

We also remain focused on growth and continue to evaluate opportunities in our pipeline.

With that, I would like to turn the call over to David to review our financial results for the quarter. David?

David N. T. Watson

Thanks, Rob, and good morning, everyone. I will discuss our financial performance for the quarter then provide an update on our balance sheet and liquidity. But first, I'd like to remind everyone that all dollar amounts expressed in today's call are in US dollars, unless stated otherwise. Facility service revenue for the quarter totaled \$96.4 million a slight increase compared to the third quarter of last year, which, as Rob mentioned, benefit from a strong recovery in cases after pandemic restrictions were lifted. Our case volumes are down 2% from the same quarter last year, although inpatient cases declined 21%. Outpatient cases were up 0.7% and observation cases increased by 31.6%.

Our total revenue and other income for the quarter was \$99 million, an increase of \$0.2 million, or 0.2% from \$98.8 million for the same period in 2020. Government stimulus income was in line with the same period last year. Operating expenses for the quarter totaled \$82.5 million, representing an increase of \$1.2 million or 1.5% compared to the third quarter of last year.

Consolidated salaries and benefits were higher as a result of annual increases, as well as industry wide labor market pressures. The most significant expense was higher share based compensation costs, which increased by \$1.4 million, driven by a strong appreciation in our share price. The percentage of total revenue and other income operating expenses increased to 83.3% from 82.2% for the comparable period. EBITDA for the quarter was \$23.3 million, or 23.6% of revenue, compared to \$24.6 or 24.8% of revenue in the third quarter of last year. During the quarter we generated cash available for distribution totaling CAD 7.5 million, resulting in a payout ratio of 29.2% compared to 17.1% in the prior year. We approached the end of the year with a strong balance sheet, improved financial flexibility and cash flow performance. As of September 30, we had approximately \$63 million of cash and equivalents. The outstanding balance in our corporate line of credit was \$31 million at quarter-end. Inclusive of lease liabilities, our net debt to equity stands at 0.51. We continue to be very well-resourced to capitalize on potential growth opportunities, and our leverage remains significantly lower than our US trading peers. I mean whether the most significant impact of the COVID pandemic, we believe we are well-positioned to increase the returning capital to our shareholders as indicated by a 15% increase in our quarterly dividend announced this morning, as well as our intention to file for accrual of a normal course issuer bid of up to 5% of the corporations issued an outstanding common shares. This concludes my Financial Review for the quarter. For additional detail on our financial results including specific results for each facility, please refer to our MDA. With that, we'd now like to open the line for questions. Operator?

QUESTION AND ANSWER SECTION

Operator

And we will hear first from Endri Leno with Canada National Bank.

Unidentified speaker

Question – Unidentified speaker: Hey. Good morning. Thanks for taking my questions.

Thank you for taking my questions. I'll start with the first one. Where are the cases or where were they in Q3 versus the pre-pandemic?

Answer – Unidentified speaker: So compared to pre-pandemic, a surgical case volume is down for the quarter 6% compared to 2019. Go ahead.

Unidentified speaker

Question – Unidentified speaker: Well I was just going to ask, I mean so that 6% pre-pandemic and then you're adding another 2% from last year or does it 6% below also include that there's a 2% decrease that you saw from last year.

Answer – Unidentified speaker: Not sure I understand the question and we're down on a quarter to quarter basis third quarter of 2021 is down 2% compared to the third quarter of 2020 and compared in 2019 we're down 6%.

Unidentified speaker

Question – Unidentified speaker: Okay. Okay. Now that's great. That's good to come there.

Answer – Unidentified speaker: Well it's a little color around that we called out, you know it was a strong third quarter last year as all the restrictions lifted and there was quite a bit of volume that was coming through. Additionally you know we've seen the Delta variant this third quarter was an issue, and then we called out some provider after a pretty couple of strong quarters we had some providers that just took a break after restrictions were lifted. So that's just sort of some added flow there.

Unidentified speaker

Question – Unidentified speaker: Okay. Thank you. And would you say those are also the main reasons why you are not yet at pre-pandemic levels or is there any more deferred care or are the surgeries being performed elsewhere?

Answer – Unidentified speaker: No, I think this is quickly. We know that there are deferred care. We see that a little bit and you see that in some of the payer mix changes, typically higher acuity cases are deferring through a difficult surge with the Delta variant, so there will be some additional cases for that. So we're not seeing any issues on the outmigration for that.

Unidentified speaker

Question – Unidentified speaker: Okay. So we can, I mean, reasonably expect to return to pre-pandemic levels, assuming there are no more surges and things of that nature?

Answer – Unidentified speaker: Yeah. Assuming we don't have another COVID surge or another outbreak on that, I mean, we continue to – continues to recover. As I said, it was just a unusual quarter, after two strong quarters we sort of took a pause. We look – looking where we are right now it looks pretty good going into the fourth quarter where we're fairly cautiously optimistic on the fourth quarter.

Unidentified speaker

Question – Unidentified speaker: Okay. No. Thank you. At least (00:10:54) my next question, I mean, that's good color for Q4. I mean, are you able to share any more details there, like would you be 95% below or closer to a 100% in Q4 so far? I don't know if you can share that.

Answer – Unidentified speaker: No. Really we're not there yet, Endri. I think we just we've got a little bit of visibility, of course, on October and it looks like typically the way our seasonality goes, it is longer – closer to the latter half of the quarter it continues to pickup with December historically being the most significant part of that. So right now we're seeing early indications that we're going to be in line.

Unidentified speaker

Question – Unidentified speaker: Okay. All right. Thank you. My next question is it relates to the dividend increase and the question I have is that if you are not been in to pre-pandemic levels but, let's say, we expect them sometime next year, but why increase the dividend at this point and not wait until you get back to 2019 levels?

Answer – Unidentified speaker: Yeah.

Nineteen levels. Yeah, Endri. That's a good question. I think when you look at our balance sheet or our balance just continue to strengthened. Debt level continues to go down. We got plenty of capacity in our line of credit and our cash position is really good. So we felt it is the right time given the strength in balance sheet and our comfort with the outlook going forward, we didn't feel it was necessary to continue waiting.

Unidentified speaker

Question – Unidentified speaker: Okay. That's good. And as I tie – I'm going to I'm going to tie that dividend increase and then you're saying the improving balance sheet, which it has and it's great. But are you seeing any changes in growth opportunities be it either for M&A or perhaps expansion?

Answer – Unidentified speaker: No changes. We feel again our objective is a competitive and a sustainable dividend and along with the ability to fund our growth projects. Our pipeline does remain very active and very and you look at a lot of opportunities and you pass on that the de novo that we've called out before take time to develop and syndicate and develop the relationships to move forward. And so, we don't see any changes in the opportunities, if nothing we've seen as an increase in that.

Unidentified speaker

Question – Unidentified speaker: Okay. Thank you. Are you able to provide any color like, let's say, versus vis-à-vis last quarter like Q2? I mean, have you advanced any more allies or have any talk, any discussions on a new de novos move forward and any color you can share there?

Answer – Unidentified speaker: Yeah. We have quite a few discussions, Endri and quite honestly in the acquisition especially in this business, you're partnering with physicians and there's been a lot of cases, healthcare systems and some opportunities just take time to germinate and gain enough interest to move forward, and some quite honestly don't materialize, so the activity around that is significant along with due diligence and things like that. So we walk away from a whole lot more than we actually get brought to ground. But again it continues to develop and our pipeline is still very active.

Operator

We will now move on to our next question from Chelsea Stellick with IA Capital Markets.

Unidentified speaker

Question – Unidentified speaker: I'm basically keeping my questions I think Endri asked most of them, but just in terms of the outpatient cases, they seem to be in line with what was in the past. But I'm just wanting additional color on why we saw the 21% decrease in inpatient cases.

Answer – Unidentified speaker: I think Hey, Chelsea it's David. You know, Rob touched on it with the part of I think it's the spike in COVID cases. And some of those higher acuity cases which is holding back and just they're starting to defer that care temporarily. But in addition there is more of a trend to cases being done and on as outpatient cases so there's some of that also.

Unidentified speaker

Question – Unidentified speaker: And is that something we're probably going to see next quarter like a continuation of outpatient cases growing and inpatient cases kind of being constrained?

Answer – Unidentified speaker: You know, when you look at year to date, it's less, Last on a year-to-date basis the inpatient case volume is down just a little bit under 9%, so right now it seems to be a third quarter phenomena. I don't anticipate that we'll see the same level that we saw in the third quarter.

Unidentified speaker

Question – Unidentified speaker: Okay. All right. Thank you. And I guess just the last one. Is it safe to say that that we see de novo AFC developments coming in before any large acquisition in the next six months sort of just over...

Answer – Unidentified speaker: Yeah. Sure. Sure. I'll just say again we've got a lot of opportunities that we're looking at and I just really wouldn't put a timeframe on that right now.

Unidentified speaker

Question – Unidentified speaker: Okay. Great. Thank you so much.

Operator

We do have a follow-up question from Endri Leno with Canada National Bank.

Unidentified speaker

Question – Unidentified speaker: Hey. Thanks for the follow-up. Just one last one for me, if you guys can talk a bit about labor tightness and how we you if at all, especially nursing that we hear is pretty tight out there.

Answer – Unidentified speaker: No, I don't think that's good question, Endri, and certainly very topical right now across the labor market in general and specifically healthcare. I'd just tell you that there – obviously there are pressures on wage right now of retention and we're not unique. Healthcare is not unique. It's not really necessarily even geographic is fairly widespread. And right now I would tell you that we will see some near-term pressure on costs. We don't have any barriers right now, though we don't expect any impact we don't expect any impact going into the fourth quarter but we'll probably see a little bit of headwind on some interim costs as to make sure that we still

maintain our staffing. But there's definitely that we also agree, I think for the most part when our peers have called us out to expect that that will hopefully normalize into 2022 but it's a little bit of a headwind on the near-term.

Unidentified speaker

Question – Unidentified speaker: Okay. All right. Thank you. That's it for me. Thanks.

Answer – Unidentified speaker: Yeah.

Operator

Well, now hear from Doug Loe with Leede Jones Gable.

Unidentified speaker

Question – Unidentified speaker: Yeah. Yeah. Good morning, gentlemen. Thanks for taking my question. Just kind of following on from Endri's question about labor market constraints, in your MD&A you flagged that Sioux Falls experiencing softness in worker compensation surgical cases and it strikes me as though that might be a trend that could also continue into 2022, so just kind of wondering what sort of trends you might be seeing on softness in that category of procedure and whether or not that might not be necessarily specific to Sioux Falls going forward?

Answer – Unidentified speaker: Doug, right now, I think it's a one quarter aberration. I'm not ready to say that's an ongoing trend. I think we'll continue to monitor carefully. But it certainly has had some impact in the quarter, but not something that we're anticipating it's going to be an ongoing issue.

Unidentified speaker

Question – Unidentified speaker: Okay. Yeah. Thanks. That's it from me.

Answer – Unidentified speaker: Thank you.

Operator

Next question will come from Sahil Dhingra with RBC Capital Markets.

Unidentified speaker

Question – Unidentified speaker: Hi. This is Sahil Dhingra for Douglas Miehm. I had one question, in terms of the government stimulus it has increased quarter-over-quarter I had one question. In terms of the government stimulus, it has increased quarter-over-quarter. Do you have any timeline or what would be the future run rate for this?

Answer – Unidentified speaker: Yeah. So the government stimulus was a little under \$200,000 on quarter-over-quarter basis. We currently have about \$1.5 million that's deferred on the balance sheet and will be recognized in future quarters. Beyond that, pending some new stimulus program, we don't anticipate seeing ongoing stimulus.

Unidentified speaker

Question – Unidentified speaker: Thank you.

Answer – Unidentified speaker: Sure.

Operator

And at this time, there is no additional questions. I will turn the call back over to Robert Horraro for closing remarks.

Thank you. In closing, we'd like to thank our physician partners, nurses, and all team members who deliver outstanding care to patients each and every day. And as always, we look forward to reporting on our progress again next quarter.

Operator

With that ladies and gentlemen, this does conclude your conference for today. We do thank you for your participation. You may now disconnect.

Call ended