Q4 2020 Medical Facilities Corp Earnings Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Endri Leno, National Bank Financial, Inc., Research Analyst

PRESENTATION

Operator

Good morning, everyone. Welcome to the Medical Facilities Corporation 2020 Fourth Quarter Results Conference Call. (Operator Instructions) Before turning the call over to management, listeners are reminded that certain statements made 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 additional information about factors that may cause the 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, 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 1 hour following the completion of the call. Details of how to access the webcast replay are available in this morning's news release announcing the company's financial results.

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

Robert Oreon Horrar, Medical Facilities Corporation – President & CEO

Thank you. Good morning, and welcome to our fourth quarter 2020 earnings call. Joining me today is David Watson, our Chief Financial Officer. Earlier this morning, we released our fourth quarter and year-end results. Our news release, financial statements and MD&A are available on our website and have been filed with SEDAR.

I would like to start by expressing my gratitude to our physician partners and all of our health care associates who continue to deliver outstanding care to patients each and every day. We are incredibly proud of how well they managed challenges of this past year.

There are a few key takeaways that I will cover in my remarks today. First, our case volumes continue to recover and are closer to pre-COVID levels. Second, we continue to benefit from decisions we made both prior to and during the pandemic. And third, we are well positioned to capitalize on market opportunities as the recovery continues.

2020 got off to a strong start. However, by the second half of March, COVID-19 had begun to surge. As a result, stay-at-home orders and temporary succession of elective cases were implemented, which had a material impact on our business; most significantly in April and May. The third quarter saw a dramatic rebound in case volumes and volumes continued to normalize throughout the fourth quarter despite the higher prevalence of COVID-19 across the United States.

Notably, hospital surgical case volume dropped to 36% of the prior year in April, but rebounded to 94% in the fourth quarter. Despite the improvement, however, COVID continued to impact our volumes during the fourth quarter as some patients deferred care.

The second quarter dropping cases and the following recovery was even more dramatic in our ambulatory surgery centers. Last April, our ASC case volumes were only 8% of prior year. But in the fourth quarter, they improved to 90% of fourth quarter 2019 levels. Our ability to recover quickly was due to the hard work and commitment of our partners and associates to ensure that our facilities continue to provide a safe environment for patients and staff.

Of critical importance was the government relief funding that our hospitals and ASC's received at various times throughout the year. These funds, in addition to the changes we made to our dividend, retirement of our debentures at the end of 2019 and selling down our position in Unity Medical, allowed us to weather this unprecedented storm as well as we did.

Despite the challenges of the pandemic, our balance sheet remains strong, as David will speak to in a moment. And as a result, we are better positioned to capitalize on growth opportunities as the recovery continues to unfold throughout 2021. I will discuss this further as well as our outlook for the year later in the call.

Now I would like to turn the call over to David to discuss our financial results for the quarter and the year.

David N. T. Watson, Medical Facilities Corporation - CFO

Thanks, Rob, and good morning, everyone. As usual, a reminder that all dollar amounts expressed in today's call are in U.S. dollars, unless otherwise stated. I will discuss our fourth quarter and year-end financial performance, then provide an update on our balance sheet and liquidity. For the year, total revenue and other income from continuing operations was $389.9 million, down 2.1% from fiscal 2019.

The 2020 figure included $26 million in government stimulus income received by our surgical hospitals and ASC's. The year-over-year decrease was primarily due to the decline in case volume, especially earlier in the year when the pandemic forced facilities to reduce selective surgeries, or temporarily cease operations. In addition to the pandemic affecting electric procedure volumes, the fourth quarter of 2019 included cases from 2 Rivers in Central Arkansas Surgical center, whereas the fourth quarter of 2020 did not.

As Rob mentioned, we saw a dramatic rebound in case volumes in the back half of the year. However, they did not reach prior year levels. On a same-store basis, total surgical cases were down 7.1%, outpatient cases were down 8.8%, and inpatient cases declined 9.2% from the fourth quarter of 2019. Observation cases, on the other hand, increased by 26.8%. The in the fourth quarter, we had total revenue and other income of $109.5 million, which included $2.4 million of government stimulus income. This was 3.9% lower than the same period last year.

Excluding transaction costs and the sale of the controlling interest in UMASH, adjusted EBITDA for 2020 was $96.1 million. This is a decrease of 0.2% from prior year adjusted EBITDA, excluding the $22 million noncash goodwill impairment charge. As a percentage of revenue, adjusted EBITDA in 2020 improved to 24.7% compared to 24.2% in 2019.

In the fourth quarter, we had EBITDA of $28.4 million, down 13.1% from the fourth quarter of last year. Our EBITDA margin for the quarter decreased to 26% of revenue from 28.7% in 2019. The decline was mainly due to lower case volumes, which translated to lower income from operations at most of the facilities.

For the year, cash available for distribution totaled CAD 40 million, resulting in a payout ratio of 21.8%. And for the quarter, we had cash available for distribution of CAD 10.1 million; resulting in a payout ratio of 21.5%. Importantly, despite the challenges of the pandemic and largely the result of decisions we made in the months leading up to the pandemic, we have a very strong balance sheet as of year-end.

At year-end, our corporate debt outstanding stood at $38 million, down from $84.8 million at the end of 2019. On a consolidated basis, total long-term debt, excluding lease liabilities, decreased by $53.7 to $97.7 million and cash and cash equivalents totaled $66.2 million. $23.2 million of the cash balance represents advances from Medicare that will be offset against future billings.

Our net debt-to-EBITDA as of year-end was [0.33]. The year-end consolidated net working capital declined to $45 million compared to $71.5 million in the year before. The change resulted from the sale of the controlling interest in UMASH in February 2020 and its underlying real estate assets in June as well as the payer advances and government stimulus funds repayable recognized in current liabilities. This was partly offset by the receipt of government stimulus funds by the facilities and cash proceeds from the UMASH sale transaction.

As of year-end, we had cash and cash equivalents of $66.2 million and $112 million available on our $150 million credit facility. This concludes my financial review. For additional detail on our financial results, including specific results for each facility, please refer to our MD&A.

I would now like to turn the call back to Rob to provide a few comments on our outlook before we open the call for questions.

Robert Oreon Horrar, Medical Facilities Corporation – President & CEO

Thanks, David. Last September, we announced the opening of St. Luke's Surgery Center, Chesterfield and Missouri. This is a de novo ASC and offers 6 specialties; including orthopedics, gynecology, GI, plastic surgery and general surgery. We're happy with the early performance of the St. Luke's ASC and expect cases to continue to ramp up throughout 2021.

The ambulatory surgery centers are an important part of our growth thesis, whether through acquisition or development of new centers. Ambulatory care is one of the fastest-growing and higher-margin segments of the United States healthcare industry. Patients prefer the accessibility and lower costs afforded by ASC's. And on top of that, the pressure on acute care hospitals during the pandemic highlighted the important role that ASC's can play in the healthcare landscape by providing an alternative and safe site for a growing list of surgical procedures.

MFC is well aligned with the expected growth in the ASC space. Our balance sheet remains strong, and we are well positioned to capitalize on potential market opportunities. We believe that there is even more opportunity coming out of COVID, and we have a robust pipeline of acquisition targets and potential de novo projects that we continue to review.

With that, we would now like to open the line for questions. Operator?

QUESTIONS AND ANSWERS

Answer – Operator: (Operator Instructions) Your first question comes from Endri Leno of National Bank.

Answer – Endri Leno: Congrats on the recovery of volumes in Q4. I had a couple of questions. I mean, first off, I'll start. Rob, you mentioned in your prepared remarks that there were some case surgeries postponed in Q4. I was wondering if you can talk a little bit more about them in the sense that if we were to normalize Q4 results from these, where would your overall case volume be in Q4? How quickly do you think these cases will be rescheduled? Or have any of them already?

Answer – Robert Oreon Horrar: Yes, that's a good question, Endri, and thank you. So we're really talking about patients who are reticent to come for either a clinic visit or even have surgery. We've seen, as we've talked about, the ebb and flow, and actually more the flow of COVID through the fourth quarter. We know those cases are there. Our facilities, and we really can't measure that, but we know it's there just episodically. So coming out of COVID and as the vaccines roll out, we expect that to return. It's hard to calculate exactly what that is, but we do know there is some demand in some cases.

I'll tell you, for the most part, those who truly needed urgent care and treatment, got it. But there'll be some deferred care. And we're not alone in that. I think every healthcare system is in the same boat with that.

Answer – Endri Leno: Okay. Great. My second question is that -- I mean, you also mentioned in the prepared remarks that it was also a bit touched upon in the Q3 call. Is that of the possibility of picking up cases from acute care hospitals? Was this the case in Q4? I mean, do you think you saw any volumes because of that? And does this still hold true for 2021 as the pandemic sort of recedes and fades?

Answer – Robert Oreon Horrar: Yes. Actually, it was the case in Q4. Certain -- some hospitals were limiting elective cases and scheduled cases as COVID admissions increased in their facilities. We did have a number of our facilities that benefited from physicians, even those that were employed by other health systems that brought cases to our facilities. The experience was outstanding. The patient satisfaction was extremely high and comments that we received is they'd like to continue to do that.

Don't really have any numbers to put to that rolling forward, but it was a positive experience. As we called out in our ASC space, the same thing applied to the ASC's, where those cases couldn't get done in the hospital. We did get a benefit in the ASC space.

Answer – Endri Leno: Okay. Great. And last one for me, I'll jump in the queue. But if you can talk a little bit about OSH, I mean what was happening there? I mean you had revenue down, but expenses were up, and then they had this default on their debt. I mean, first of all, what's happening there? Then what is the outlook for that hospital in Q1 or for the rest of 2021?

Answer – David N. T. Watson: Yes. Endri, it's David. So in Q4, OSH had weak volume, they were down about 9%. That corresponded to about a 10%

drop in their revenue. And on the expense side, they've seen -- they've had fairly high health benefits expense, primarily COVID-related, and that had an impact on the quarter.

Consequently, when you look at the results for the quarter, it had an impact on their ability to meet their covenants, they tripped the covenant. And as a result of that, they paid down the debt subsequent to year-end.

Answer – Endri Leno: So how does that situation look then now in Oklahoma? Has it improved at all? Or does it continue to be similar to Q4?

Answer – Robert Oreon Horrar: No. I think this is a single -- again, this is primarily predominantly a spine hospital with orthopedics. The outlook, I think we think we're very optimistic on that. It will return. COVID was a big issue here. So coming out of all of that, the outlook for us, we're very optimistic we'll return and be back to normal.

Answer – Operator: (Operator Instructions) There are no further questions. I will now return the call to Mr. Horrar for closing comments.

Answer – Robert Oreon Horrar: Thank you for joining us on today's call and for your continued interest in MFC. As always, we look forward to reporting on our progress again next quarter. Thank you.

Answer – Operator: Ladies and gentlemen, this concludes today's conference call conference call. Thank you for participating. You may now disconnect.
