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Agilon Health, Inc. (AGL)

Q2 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello, everyone, and welcome to the agilon health Second Quarter 2021 Earnings Conference Call. My name is Brika, and I'll be the moderator for today's event. [Operator Instructions]

And I will now hand over to Matthew Gillmor to start. So, Matthew, please go ahead when you're ready.

Matthew Dale Gillmor
Vice President, Investor Relations, Agilon Health, Inc.

Thank you, Brika. Good morning, and welcome to our second quarter conference call. With me this morning is our CEO, Steve Sell; and our CFO, Tim Bensley. Following prepared remarks from Steve and Tim, we will conduct a Q&A session.

Before we begin, I'd like to remind you that our remarks and responses to questions may include forward-looking statements. Actual results may differ materially from those stated or implied by forward-looking statements due to risks and uncertainties associated with our business. These risks and uncertainties are discussed in our SEC filings. Please note that we assume no obligation to update any forward-looking statements. Additionally, certain financial measures we will discuss in this call are non-GAAP financial measures. We believe that providing these measures helps investors gain a better and more complete understanding of our financial results and is consistent with how management views our financial results. A reconciliation of these non-GAAP financial measures to the most comparable GAAP measure is available in the earnings press release and Form 8-K filed with the SEC.

With that, I'll turn the call over to Steve. Steve?

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

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Thanks, Matt. Good morning, everyone, and thank you for joining us. We're hosting today's call from Austin, Texas. Before I get to the details of our quarter, I'd like to take a minute and talk about our experience in this important market and how it demonstrates the power about what agilon has built with our physician partners.

In 2018, agilon entered the Austin market in partnership with Austin Regional Clinic, the largest independent multispecialty group, and Premier Family Physicians, the second largest independent primary care group in the region. In 3.5 years, our partnership has expanded access to top quality care in Austin by adding physicians, increasing clinical team-based support and analytics, and opening previously closed primary care panels to new senior patients. Our Austin membership has expanded at a compounded annual rate nearly double the local growth in the Medicare Advantage program, all while dramatically improving quality and generating world-class patient experience scores. Last year, we expanded with two new anchor partners in East Texas that are currently in the implementation and will go live in 2022. Our Austin experience of local and now statewide growth in independent primary care and the resulting benefits in terms of senior patient care, quality and access is an experience that we can see replicated further in Texas and in numerous communities and states across the country.

Now, with the focus of our call. I will cover four areas in my prepared remarks. First, some highlights from our second quarter results; second, our collaboration in recently launching Primary Care for America; third, an update on our progress in driving growth for new markets in 2022 and 2023; and finally, I'll wrap up with some comments on Direct Contracting. Starting with a few highlights from the second quarter. We were pleased with our performance this quarter. Revenues increased 70% on a reported basis and were up 58% normalized for retroactive membership from the first quarter. Membership increased 45%, and same geography membership growth was up 17%. Our same geography growth approach is distinctive and highly efficient as it is driven by strong retention, patients within existing panels choosing Medicare Advantage or new physicians joining our anchor partners on the platform. This quarter's strong growth was amplified as investments in technology and tighter operational alignments with health plan partners accelerated the pull-through of attributed senior patients in our partner practices.

We have added a record number of members to the agilon platform in 2021, and we now support more than 280,000 senior patients. This includes 33,000 members added January 1 of this year from new geographies in Hartford, Buffalo and Toledo; 20,000 members to existing partners in our Same Geographies; more than 50,000 attributed Direct Contracting beneficiaries added on April 1; and finally, 49,000 Medicare Advantage members currently in the implementation for January 2022. This compares to approximately 115,000 live and implementing members on the platform at the end of 2019. This incredible growth reflects the flexibility of our purpose-built platform to onboard and serve, at scale, a diverse set of groups and geographies and the demand among health care stakeholders for innovative primary care-centric delivery models.

At the same time, our partners are growing their Medicare Advantage membership. We are seeing a strong trend of growth in underlying medical margin. With our Q2 results, medical margin has advanced to $100 per member per month year-to-date in 2021. This is down from last year due to COVID, which significantly depressed utilization, particularly in Q2 of 2020, but overall medical margin is up from the same year-to-date period in 2019. We have made this progress despite the temporary dilution from the new members on the platform, indicating a very strong improvement from our earlier cohort patient groups. Additionally, over the same period, we've driven substantial leverage against our platform support, resulting in improvement in our adjusted EBITDA.

Turning now to the launch of Primary Care for America. In late June, we partnered with ten leading health care organizations, including the American Academy of Family Physicians and American College of Physicians, to form this new group intent on influencing government health policy. This collaboration is focused on

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demonstrating the value of primary care and the need for increased investment in innovative payment models. The recent report from the National Academies of Sciences outlines primary care as the only discipline of medicine where a greater supply results in better health outcomes, along with longer life expectancy and lower costs. In the coming months, Primary Care for America will engage policymakers through a series of briefings, recommendations and roundtable discussions.

Now, let me turn to our progress on driving growth in new markets for 2022 and 2023. As we have previously discussed, the class of 2022 includes six physician partner groups with 49,000 Medicare Advantage members, including the two groups in East Texas I mentioned earlier. As a reminder, these members are on our platform, but won't start generating revenue until January of next year. The class of 2022 includes a diverse set of geographies, both in terms of new and existing states as well as different levels of MA penetration and plan mix. We've made strong progress implementing these new geographies by hiring local leadership and completing the initial technology and data integration with multiple new electronic medical record and payer systems.

Annual wellness visits are tracking in line with our plan, and we continue to make strong progress on contracting with new health plans in the six markets. With respect to the pipeline for new partners in 2023, our business development team has made great progress in the last couple of months. The pace and tempo in this work is very encouraging with signed letters of intent or advanced dialogue with multiple groups in new markets, both in existing and new states. This development work will continue through the back half of this year. And while we will share more holistic details in future calls, we remind you that implementation for signed letter of intent groups will begin in the coming months. Within the class of 2023, we are seeing higher levels of interest in operating an integrated Medicare line of business, encompassing both Medicare Advantage and Direct Contracting.

And each of these groups is compelled by the opportunity to shift their senior patients to a subscription-based Total Care Model. With the additions from the class of 2022 and the strong 2023 prospects, our network continues to grow at impressive rates. And we are leveraging this breadth to share best practices, accelerate onboarding and improve outcomes for senior patients, our partners and agilon. In late July, we gathered with 60 physician partners for three days in Traverse City, Michigan for a retreat. We were hosted by one of our new partners, and the gathering included all of our existing partners, the entire class of 2022 as well as potential members of the class of 2023. The energy and enthusiasm from our partners for transforming senior care in their communities was palpable.

Let me close by providing an update on Direct Contracting. We have been pleased with our initial performance in this new program. While it's still early, our launch has gone relatively smoothly. And attributed membership and adjusted EBITDA came in modestly above our initial expectations. Importantly, our physician partners are already noticing the benefits of operating consistently across the entire Medicare line of business. Over the past several months, we've been able to spend time with the Medicare Innovation Center as well as members of Congress and other interested stakeholders to discuss the program. We've been encouraged with the dialogue and hope to advance policies that could improve the sustainability and predictability of the program. As I've said on prior calls, government programs change over time, but we continue to believe Direct Contracting is fundamentally aligned with the administration's goals of improving equity and access to primary care delivery models. Over the next few months, we will formalize our plans for participating in the Direct Contracting program with new and existing partners in 2022, and we expect to update you on those decisions in our next call.

With that, I'll now turn the call over to Tim.

Timothy S. Bensley
Chief Financial Officer, Agilon Health, Inc.

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Thanks, Steve, and good morning, everyone. I'll review some highlights from our financial statements and provide some additional details on our guidance for the third quarter and full year 2021, starting with membership. Membership increased by 45% on a year-over-year basis during the second quarter to approximately 182,000. Membership growth was driven by a combination of same geography growth and the impact in three new geographies that went live in January. Same geography membership growth was 17% for the second quarter. Similar to last quarter, same geography growth was broad-based across markets with all of our Same Geographies growing at or above the national growth rate for Medicare Advantage enrollment. Average membership was approximately 194,000 during the quarter, which was up 57% from last year. It's important to keep in mind that our average membership metric includes 13,000 retroactive members attributed to the first quarter. This retro impact reflects the large group contract we mentioned on the last call. Additionally, as Steve referenced, average membership benefited from faster member attribution during the quarter, which drove some additional retro impact.

Revenues increased 70% on a year-over-year basis to $499 million. Year-to-date revenues increased 56% to $912 million. Second quarter results include $35 million in retro revenue associated with the first quarter. Excluding this, revenue growth would have been 58% in the quarter. Revenue growth was primarily driven by membership gains from new geographies and Same Geographies. On a per member per month basis, or PMPM, revenue increased 8.5% during the second quarter. The increase to revenue PMPM was primarily driven by updates to CMS county benchmarks, changes in member acuity or burden of illness and one extra month of sequestration suspension relative to prior year. Additionally, revenue PMPM was also impacted by a few year-to-date true-ups and the mix impact from retro members. Revenue PMPM growth would have been closer to 6% normalized for these true-ups, retro mix and the sequestration benefit.

Medical margin was $55 million during the second quarter compared to $72 million in the prior year. On a year-to-date basis, medical margin was $107 million compared to $114 million during the same period last year. The year-over-year decline in medical margin reflects the lower utilization in prior year due to COVID, which more than offset the positive impact from clinical programs and the maturation of members on the platform. Medical margin on a PMPM basis was $95 during the second quarter compared to $195 in the prior year but was roughly consistent with $106 in the first quarter of 2021.

Network contribution, which is defined as medical margin after surplus sharing with our physician partners, was $24 million during the second quarter compared to $39 million in the prior year. On a year-to-date basis, network contribution was $54 million compared to $63 million last year. The year-over-year decline in network contribution primarily reflects the COVID impact on prior year medical margin. Platform support costs, which include market and enterprise level G&A, increased 22% to $31 million. On a year-to-date basis, platform support costs increased 21% to $59 million. The growth in our platform support cost remains well below our revenue growth, which highlights the light overhead structure of our partnership model. As a percent of revenue, platform support was 6% during the second quarter, down from approximately 9% in the prior year. On a PMPM basis, platform support declined approximately 20%.

Adjusted EBITDA for the quarter was negative $2 million versus positive $14 million in the prior year. On a year-to-date basis, adjusted EBITDA was positive $2 million compared to positive $16 million last year. The year-over-year change to adjusted EBITDA reflects dynamics we previously discussed for medical margin. This was partially offset by leverage against platform support costs and contributions from Direct Contracting, which is included in other income. Turning to our balance sheet and cash flow. We ended the quarter with $50 million in debt outstanding and $1.1 billion in cash, which reflects proceeds from the initial public offering we completed in April. Cash flow from operations was negative $39 million in the quarter, which included a $12 million premium payment

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for public company D&O insurance, $10 million in geography entry costs and capital support, $8 million in annual incentive comp as well as $4 million in severance expense triggered by the IPO.

Turning to our financial guidance for the third quarter and full year 2021. For the third quarter, we expect ending membership in a range of 183,000 to 184,000 and revenue in the range of $450 million to $453 million. The sequential decline in revenue from second quarter result to third quarter guidance is primarily due to the revenue from retroactive membership that we recognized in the second quarter. For the full year 2021, we have increased our ending membership outlook to a range of 184,000 to 185,000 and our revenue outlook to a range of $1.81 billion to $1.82 billion. We continue to expect adjusted EBITDA loss of $41 million to $38 million. We expect the adjusted EBITDA loss will be somewhat weighted to the fourth quarter. This is due to normal seasonality and our expectation that utilization will approach pre-COVID levels as we move through the year. Additionally, our adjusted EBITDA outlook reflects the temporary dilution from higher membership growth and an unchanged view of full year profitability for Direct Contracting.

With that, we're now ready to take your questions. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question we have comes from Stuart Hill (sic) [George Hill] (18:02) from Deutsche Bank. Mr. Stuart (sic) [George] (18:04), your line is open. Please go ahead when you're ready.

George Hill
Analyst, Deutsche Bank Securities, Inc.

Q

Good morning, guys. And that's George Hill from Deutsche Bank. And I appreciate you guys the question. I guess, could you talk a little bit more about attribution as a driver of the strong membership number in Q2? And then a quick kind of follow-up question would be, the other medical expense kind of came in a little higher than we expected. I know it's kind of a small number but would just love any incremental color that you can provide around that.

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

Sure. Thanks, George. I'll take the first one, Tim, and you can take the second one. So, George, I think we're really pleased with our strong growth in the quarter. Attribution, I think, is something that we do really well and is a distinctive part of our model. It allows us to work very closely with health plans and get more members attributed to our partners. We are making investments in technology and working on operations with our health plan partners to do that. And so, the biggest driver of the step-up from the 15% same geography growth to the 17% that you saw in Q2 really was around attribution. These are members that typically we might have expected to bring on the platform in the back half of the year. But by getting a better process and the technologies, we were able to pull them into the first half of the year. And as Tim shared in his remarks, they are retroactive to January 1 of this year. I think that was about 3,100 of the members that you see within the retro activity. So, area of strength, one that we think we're getting better at all the time. Disproportionate amount of those numbers are PPO, which is an area of strength for us. So, hopefully, that gives you context.

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Timothy S. Bensley
Chief Financial Officer, Agilon Health, Inc.

A

Yes. Thanks, George. And overall, the medical margin number on a PMPM basis that were reported in the quarter of $95, and as Steve said, the overall medical margin PMPM year-to-date of $100 is pretty much in line with where we expected it to be. And that $100 obviously is down versus prior year because of the...

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

[indiscernible] (20:11) other medical expense.

Timothy S. Bensley
Chief Financial Officer, Agilon Health, Inc.

A

Other medical – oh, I'm sorry, I thought we were talking about – other medical expense were up. Overall, other medical expenses essentially are – include our AWV incentives that we pay to our physician partners. That can be kind of lumpy on a quarter-to-quarter basis depending on when those AWVs happen and when we pay those incentives. So, when the number is up, it means that we're – as Steve was talking about, we're actually in really good shape so far in getting our AWVs completed earlier in the year and then paying those incentives out. And I can talk more about the medical margin year-over-year if you want to, too, George.

George Hill
Analyst, Deutsche Bank Securities, Inc.

Q

Well, you know what, that's great color. I'll pause there and I'll hop back in the queue, and I'll let other people ask some questions. Thank you.

Operator: Thank you. The next question comes from Kevin Fischbeck of Bank of America. So, Kevin, please go ahead.

Q

This is actually [ph] Adam (21:08) on for Kevin. But back to your comment about medical costs. It seems like you beat EBITDA in the quarter, and you don't guide to MLR, but it came in a little higher than what we were estimating, and I guess, consensus. But then you also reiterated EBITDA for the year, even though you beat. So, I was just kind of wondering thoughts on medical cost utilization patterns. And by reiterating EBITDA, are you're basically expecting higher costs in the back half? Thanks.

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

Yeah. So, I can start, and Tim can chime in. Let me first say, I think we're pleased by where we're at for medical margin. I think the biggest effect of medical margin coming in where it did is the dilution effect of the new members coming on the platform, right? There's been incredible growth. 53,000 of our members or 30% of our June 30 membership has come on since January 1 of this year. And those members – obviously, new members always will come in at lower medical margins than more mature cohorts over time. And as we look internally at that progression, [ph] Adam, (22:19) I think we're really encouraged by the improvement that we're seeing in our earlier patient cohort groups as we said in our prepared remarks.

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So, that's kind of commentary on medical margin. You've asked about EBITDA guidance in the back half of the year. I think, to paraphrase it, we're keeping our EBITDA guidance in line even though we beat in Q2, and we're reflecting higher revenues. I mean, I think the biggest parts of that – there's a few facts, the two I'd really call out is, one is what Tim talked about around Direct Contracting, right? So, even though we were higher than expected than we had initially expected in Q2, we're not changing our full year outlook on that new government program. And so, we're taking that approach as we'll get more information over the next couple of months. And then the second part is just the dilutive effect of those new members coming on. So, Tim, anything you'd add?

Timothy S. Bensley
Chief Financial Officer, Agilon Health, Inc.

A

Yeah. And if I can just quickly quantify the impact of that first Direct Contracting impact, it's – Direct Contracting contributed about $2.5 million to our adjusted EBITDA in the quarter. And as Steve said and for the factors he talked about, we expect that on the full year to migrate back to our original expectation of around breakeven for the full year. So, we're not flowing that $2.5 million through in the second half guidance.

Q

Got it, thanks.

Operator: Thank you. We now have the next question from Justin Lake of Wolfe Research. So, Justin, please go ahead when you're ready.

Harrison Zhuo
Analyst, Wolfe Research

Q

All right. This is Harrison on for Justin. Just thinking about one question mechanically on Direct Contracting. For kind of a, I guess, forward year Direct Contracting view, would you normally expect [ph] entry-year adds (24:14) from the program? I know most of its claims aligned, and so I see that seamlessly come in at the beginning of the year, but would you expect any [ph] entry-year adds (24:22) from maybe the other alignment method? And then – or would people expiring kind of contribute to a general decline throughout the year?

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

I think that we might see sort of modest adds throughout the year through the voluntary attribution process that you talked about, Harrison. The vast majority of our members are coming through that claims-based approach that you talked about. I think there will be kind of a progression that looks a little bit like Medicare Advantage throughout the year. And so, I think, we think if the – its growth will be relatively modest throughout the year for Direct Contracting, but it's early, and we're going to see sort of how it plays through.

Harrison Zhuo
Analyst, Wolfe Research

Q

Got it, thank you. Appreciate it.

Operator: [Operator Instructions] And we now have a question from Ryan Daniels of William Blair. So, Ryan, your line is open.

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Ryan Daniels
Analyst, William Blair & Co. LLC

Q

Hi, guys. Congrats on the quarter. Thanks for taking the questions. Another one on Direct Contracting, obviously, the nice contribution for a short period relative to what you expected. And I'm curious other than conservatism, what could actually bring the EBITDA down to breakeven for the full year? So, kind of turn that into a loss in the second half of the year. Are there investments or changes? Thanks.

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

Yeah. I think, Ryan, what we've got is early information from a claims and revenue perspective. We're going to be getting a lot more information here in the next month or two. So, I think it's really sort of better visibility on that, which would be the biggest driver that would drive it there. And then I think there's also just this seasonal progression that Tim talked about in his remarks, in which Direct Contracting will sort of follow the same path as MA, in which you see lower medical margin and therefore, obviously, lower overall EBITDA in the back half of the year.

Timothy S. Bensley
Chief Financial Officer, Agilon Health, Inc.

A

And just to tack on to that and like in the MA business, we do expect that utilization is going to increase in the back half of the year versus what we saw in Q2. So, we would expect that the profitability on Direct Contracting would – that would contribute to the lower profitability in the second half of the year also.

Ryan Daniels
Analyst, William Blair & Co. LLC

Q

Okay, that makes sense. And then you mentioned in your pipeline conversations with new provider groups that they're looking for more integrated Medicare solutions with both MA and DC. Is that giving you an advantage given that you're already in the DC program, one of three dozen or so, such that those that want that integrated solution have a more limited set of potential partners, given that those that aren't already in can't go into it next year? Thanks.

Steven J. Sell
President, Chief Executive Officer & Director, Agilon Health, Inc.

A

Yes. Thanks, Ryan. I think it does give us an advantage. We have five active DCEs and four more that can come online in 2022. We have the ability to add new physician groups in underneath those. And so, the ability to have this integrated full Medicare line of business is very attractive to these groups, and different MA penetration rates in different markets as we look at new states. So, we see it as a real advantage.

Ryan Daniels
Analyst, William Blair & Co. LLC

Q

Okay, thank you. I'll hop back in the queue.

Operator: We have had no further questions. I'll hand it back to Matthew.

Matthew Dale Gillmor
Vice President, Investor Relations, Agilon Health, Inc.

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Well, great. We appreciate your interest in the company. We look forward to speaking with you at future calls and future events. So, thank you.

Steven J. Sell

President, Chief Executive Officer & Director, Agilon Health, Inc.

Thanks, everyone.

Operator: Ladies and gentlemen, that does conclude today's call. Thank you all again for joining. You may now disconnect your lines.

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