LifeStance Third Quarter 2024 Earnings Script

Monica Prokocki, VP of Finance & Investor Relations

Thank you, Operator.

Good morning, everyone, and welcome to LifeStance Health's third quarter 2024 earnings conference call.

I'm Monica Prokocki, Vice President of Investor Relations. Joining me today are Ken Burdick, Chief Executive Officer and Dave Bourdon, Chief Financial Officer.

We issued the earnings release and presentation before the market opened this morning. Both are available on the Investor Relations section of our website, investor.lifestance.com.

Before turning the call over to management for their prepared remarks, please direct your attention to the disclaimers about forward-looking statements included in the earnings press release and SEC filings.

Today's remarks contain forward-looking statements, including statements about our financial performance outlook, business model and strategy. Those statements involve risks, uncertainties, and other factors, as noted in our periodic filings with the SEC that could cause actual results to differ materially.

In addition, please note that we report results using non-GAAP financial measures, which we believe provide additional information for investors to help facilitate comparison of current and past performance. A reconciliation to the most directly comparable GAAP measures is included in the earnings press release tables and presentation appendix.

Unless otherwise noted, all results are compared to the comparable period in the prior year.

At this time, I'll turn the call over to Ken Burdick, CEO of LifeStance. Ken?

Ken Burdick, Chairman & CEO

Thanks, Monica, and thank you all for joining us today.

Last month on October 10th, we observed World Mental Health Day. Within our own country, the growing disconnect between the demand and supply of mental health services remains one of the largest challenges facing Americans today. Through our mission of providing affordable and accessible mental healthcare, we at LifeStance relentlessly fight each day to mitigate this crisis.

Turning to financial performance, we are very pleased with the team's continued execution in the third quarter. For the eighth consecutive quarter, we have met or exceeded our expectations. Our revenue growth of 19%, and our disciplined execution, created solid operating leverage that yielded a 9.8% profit margin. Based on the strong performance in the third quarter, we will again be raising our full year guidance for all financial metrics.

I cannot emphasize enough the role that our clinicians have played in our achievements in the third quarter and throughout the year, as well as the value they deliver every day in providing high-quality patient care. We now have a team of over 7,200 clinicians, an increase of 285 just this quarter.

Turning to operational execution, we continue to make progress on our initiatives to streamline the business and improve performance.

First, we continued the implementation of our new operating model. As a reminder, this initiative standardizes our organization with consistent staffing and processes across our 33 states and over 550 centers. We are confident that this higher level of administrative and clinical support will position the business to scale efficiently in 2025 and beyond.

Additionally, we continue to roll out our new digital patient check-in tool. We have implemented it successfully in 11 states and expect to complete the national rollout by mid-year 2025. While still in the early stages, we are seeing higher patient satisfaction, operational efficiencies, and significant improvements in patient collections where this tool has been deployed.

Shifting to payor strategy, we are proud of the success that our payor engagement team has had in securing improved rates. While this represents progress, we still have a long way to go to achieve parity with physical health reimbursement.

As previously communicated, the third quarter is the first one where the decrease in rates from a single outlier payor with above-market reimbursement is reflected in our results. However, much of the impact of this initial rate decrease was mitigated by negotiated rate increases with other payors. Many of the new rate increases went into effect sooner than we had expected, which drove the outperformance in total revenue per visit.

Before concluding, I want to take a moment to comment on the recent hurricanes, Helene and Milton. My thoughts go out to each and every one of the LifeStance patients, clinicians, team members and the communities we serve that have been impacted by these storms. Dozens of our centers were affected, and all but two were back up and running within one week. The remaining two centers reopened by mid-October. I'm proud and appreciative of the way that our teams responded to these disasters—yet another testament to the resilience of the team and dedication to putting our patients first.

With that, I'll turn it over to Dave to provide additional commentary on our financial performance and outlook. Dave?

Dave Bourdon, Chief Financial Officer

Thanks, Ken.

Like Ken, I am pleased with the team's operational and financial performance in the third quarter.

We delivered strong top-line results with revenue of $313 million, representing growth of 19% year-over-year. The outperformance was driven by higher total revenue per visit and increased visit volumes.

Visit volumes of 2.0 million increased 15% year-over-year, driven primarily by clinician growth. In the third quarter, we added 285 net clinicians, which exceeded our expectations. This brings our total clinician base to 7,269, representing growth of 13% year-over-year. There is variability in the pace of clinician adds throughout the year. Similar to last year, we expect a lower number of net clinician adds in the fourth quarter.

With regard to clinician productivity, it came in slightly ahead of our expectations in the third quarter.

Total revenue per visit increased 3% year-over-year to $159, primarily driven by payor rate increases that came in earlier than our previous expectations, and to a lesser extent, one-time favorability.

Regarding profitability, the better-than-expected top-line results flowed through to Center Margin. Center Margin of $100 million in the quarter increased 32% year-over-year, primarily due to higher total revenue per visit, higher visit volumes, and operating leverage in center costs. Outperformance in the quarter relative to our expectations was primarily driven by higher total revenue per visit, higher visit volumes, and lower than expected spending.

Adjusted EBITDA of $31 million in the quarter was very strong and exceeded our expectations, increasing 110% year-over-year. This is the fourth consecutive quarter of doubling our adjusted EBITDA year-over-year.

Adjusted EBITDA as a percentage of revenue grew over 4 points year-over-year to 9.8%. The outperformance in the quarter was primarily attributable to the improvement in Center Margin, as well as lower than planned spending in G&A.

Turning to liquidity – in the third quarter, we generated solid free cash flow of $18 million. We exited the quarter with $103 million in cash and net long-term debt of $279 million. Year-to-date, we have generated approximately $30 million of free cash.

In the fourth quarter, we are making an enhancement to our clinician value proposition by implementing a bi-weekly payroll cycle for our clinicians who were previously paid on a monthly basis. This will have a roughly $15 million negative impact on cash in Q4 related to the change in pay periods.

Even with the impact of this payroll change, we expect to be free cash flow positive in the fourth quarter and now expect to finish the full year with meaningful positive free cash flow due to stronger year-over-year operating results, disciplined capital deployment, and progress toward resolving collection issues.

DSO improved 2 days sequentially to 47 days in the quarter. We are continuing to work through the impact from the Change Healthcare collections disruption along with some delays from a couple of payors updating their systems to reflect higher negotiated rates. These are all timing issues that we are actively working through, and we expect DSO to further improve in the fourth quarter.

We continue to see improvement in our leverage ratios, with both our net and gross leverage ratios improving nearly 50 basis points sequentially to 1.7 and 2.7 times, respectively. This represents a significant decline from 4.4 net and 5.3 gross leverage in Q3 of last year.

In terms of our outlook for 2024, we are raising our full year revenue range by $17 million at the midpoint, to $1,228 million to $1,248 million. We are also raising our full year Center Margin range by $17 million at the midpoint to $382 to $398 million and the full year Adjusted EBITDA range by $15 million at the midpoint to $105 to $115 million.

For the fourth quarter, we expect Revenue of $302.5 to $322.5 million, Center Margin of $89 to $105 million, and Adjusted EBITDA of $18 to $28 million.

Due to some of the one-time rate favorability in the third quarter, we expect modest quarter over quarter decline in total revenue per visit.

As previously stated, based on the Adjusted EBITDA outperformance so far this year, we continue to give ourselves flexibility through the remainder of the year to make additional investments to better position us to achieve our 2025 growth objectives.

Additionally, we continue to expect stock-based compensation to be at or below the bottom of our previously guided range of $80 to $95 million. This represents a significant reduction from $99 million last year.

We will open 6 de novos in 2024, with an additional 5 to 10 originally planned for this year shifting into early next year. As a result, we expect substantially higher de novo openings in 2025 and will provide specifics when we deliver guidance next quarter.

Looking ahead to 2025, I'd like to provide an early view on headwinds and tailwinds for the business.

In regard to headwinds—as a reminder, we stated we would experience downward pressure in total revenue per visit not only in the back half of 2024, but also the first part of 2025, due to the single outlier payor negotiating their reimbursement to be more in line with our overall book of business. In the first quarter, we expect the last rate drop related to that same payor negotiation.

In addition, the current CMS rate proposal for 2025 is a reduction of almost 3%. We expect to be able to offset both of those decreases by improving reimbursement with other payors, and now anticipate that our overall rate growth next year will be roughly flat.

In regard to tailwinds, we continue to see strong growth of clinicians and patient demand, which will drive visit volumes. In addition, we expect continued operating leverage.

As a result of these headwinds and tailwinds, we expect minimal margin improvement next year. We feel good about our ability to navigate and absorb challenges such as the rate dynamic while also delivering on our commitments regarding mid-teens revenue growth and exiting 2025 with double-digit margins.

With that, I'll turn it back to Ken for his closing remarks.

Ken Burdick, Chief Executive Officer

Thanks, Dave.

As we enter the final stretch of 2024, I'm looking forward to maintaining the momentum of the last eight quarters. Thanks to the tremendous dedication and commitment of the team, we have outperformed our expectations on nearly every metric this year, including revenue, adjusted EBITDA, and free cash flow. In a year with significant disruption to collections and an unprecedented rate reduction by an outlier payor, I am incredibly proud of the resilience demonstrated by our entire team.

We acknowledge that 2025 will be a particularly challenging year, due to the rate dynamics that Dave highlighted. 2024 is shaping up to be a year of very strong margin expansion. We are well ahead of schedule in delivering on our multi-year financial commitments.

As this is our last earnings call in the current calendar year, I'd like to take a moment to express my appreciation to our ten thousand colleagues who delivered the results that Dave and I have the privilege of sharing with all of you today.

We will now take questions. Operator?