LifeStance Fourth Quarter 2023 Earnings Script Outline

Monica Prokocki, VP of Finance & Investor Relations

Thank you, Operator.

Good morning, everyone, and welcome to LifeStance Health's fourth quarter 2023 earnings conference call.

I'm Monica Prokocki, Vice President of Investor Relations. Joining me today are Ken Burdick, Chief Executive Officer; Dave Bourdon, Chief Financial Officer; and Danish Qureshi, Chief Operating 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. In addition, a replay of this conference call will be available following the call.

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.

I would like to begin by highlighting what we stand for here at LifeStance. Every day we are focused on three foundational pillars—the patient experience, clinical quality, and developing an inclusive, purpose-driven culture.

First, we are committed to putting the patient experience at the forefront of everything we do. Since the start of the pandemic, the country has experienced an alarming increase in the rates of anxiety and depression, as well as deaths resulting from overdose and suicide. More than 150 million people live in an area with a shortage of mental health professionals and only 56% of psychiatrists accept commercial insurance. Tens of millions of Americans are unable to access mental healthcare treatment, with devastating effects on families and communities.

In 2023, LifeStance's team of over 6,600 clinicians helped address these access challenges by providing mental health services to over 880,000 patients who depend on our care. With our differentiated hybrid model of in-person and virtual visits, we meet patients where they are. By accepting insurance, we provide patients with affordable access to mental healthcare, whereas much of the market is cash-pay and therefore out of reach for the majority of Americans.

The exceptional care provided by our clinicians is reflected in the feedback we have received from our patients. In 2023, LifeStance received a patient Net Promoter Score of 82, and our average Google review score across all LifeStance centers stood at 4.5 out of 5 stars. As you will hear in our prepared remarks, we continue to focus on enhancing the end-to-end experience for our patients.

Second, we are dedicated to clinical quality. LifeStance and our team of multidisciplinary clinicians are committed to providing patients with personalized, high-quality care with clinical integrity. We provide training programs for our clinicians and conduct clinical audits to conform with best practice guidelines, which also afford an opportunity for our clinical leaders to collaborate with and mentor our clinicians. Our focus is on delivering the most appropriate treatment for each patient's individual needs based on informed clinical judgement.

As we enhance our capabilities around clinical quality, I am excited to announce the appointment of Dr. Ujjwal Ramtekkar as Chief Medical Officer. He joined LifeStance in January and is off to a great start. Ujjwal is board-certified in pediatric and adult psychiatry and has held multiple senior clinical leadership roles in our industry.

Last but not least, we are evolving from an entrepreneurial company focused almost exclusively on growth to one that is more balanced and disciplined when it comes to prioritization and execution. While we continue to grow as a company, we are also "growing up," to ensure that as a company we have the people, systems, processes, and culture to deliver on our mission at scale. As a leadership team, we are committed to developing a sustainable, inclusive, and purpose-driven culture that keeps our organization aligned with our vision, mission, and values.

2024 represents the second year of our two-year plan to invest in the business, fortify our foundation and standardize our operations. At the one-year mark, we are beginning to see some tangible benefits.

First, we beat on all guided metrics for the full year 2023. This quarter represents the fifth consecutive quarter that LifeStance has met or exceeded expectations across all financial metrics.

Second, we are making solid progress on our three strategic investments. We remain on track to launch both our human resource information system and our new credentialing and clinician onboarding system by this summer. For the third initiative, the electronic health record, we completed the initial discovery process where we identified incremental opportunities for improvement with our existing platform. For 2024, we are focused on those improvements and enhancing related processes. As a result, we will further evaluate our long-term EHR solution in 2025.

One example of the improvements we are making is a digital patient check-in tool that we believe will enhance the patient, clinician, and front office staff experience while reducing our administrative costs. While it is still early, we have seen encouraging results in our initial launch.

Third, we have become more strategic when it comes to our payor strategy. In 2023, we terminated roughly 30% of our 440 payor contracts. In 2024, we will continue to evaluate our payor relationships and focus on aligning with payor partners who share our vision of expanding access to mental healthcare.

And finally, we continue to remain laser-focused on profitability while making the near-term investments needed for the long-term success of the business. This was the first time in recent quarters where our revenue grew faster than our adjusted G&A. Going forward, we expect operating leverage and margin expansion to be the norm at LifeStance.

This year, we will continue to strengthen our operational processes by streamlining, standardizing, and automating end-to-end workflows. While we have made meaningful progress, there is plenty of work remaining to improve our operational and financial performance. Said differently, we have steadied the ship, but we have not yet come close to optimizing the potential of our business.

With that, I'll turn it over to Dave to provide additional commentary on our fourth quarter and full year financial performance, as well as our 2024 guidance. Dave?

Dave Bourdon, Chief Financial Officer

Thanks, Ken.

Like Ken, I am pleased with the team's operational and financial performance in 2023, exceeding our expectations for the full year.

In the fourth quarter, we achieved strong top-line results with revenue of $281 million, representing growth of 22% year-over-year, with outperformance in the quarter driven primarily by positive visit volumes as our clinicians delivered more visits during the holiday season than expected.

Visit volumes of 1.8 million increased 20% year-over-year, primarily driven by organic clinician growth and modest productivity improvements. Total revenue per visit increased by 2% year-over-year to $157, primarily driven by payor rate increases.

For the full year, we delivered revenue of $1,056 million, up 23% year-over-year.

Regarding profitability, the better-than-expected top-line results flowed through to Center Margin. Center Margin of $83 million in the quarter increased by 33% year-over-year. Full year Center Margin of $302 million grew 27% year-over-year.

Adjusted EBITDA of $20 million in the quarter was strong and consistent with our expectations. Our fourth quarter Adjusted EBITDA increased 99% year-over-year. For the full year, adjusted EBITDA was $59 million, representing 5.6% of revenue.

Turning to liquidity -- in the fourth quarter, we generated positive free cash flow of $5 million and $17 million in cash from operating activities. These improvements in cash flow were driven by higher collections, with DSO improvement of 11 days from 52 in Q3 to 41 in Q4. Each one of these days represents approximately $3 million in cash. As expected, DSO improved in Q4 as we released claims that we had intentionally held in Q3 due to positive updates from rate negotiations with several large payors.

Free cash flow and cash from operating activities were negatively impacted in the quarter due to the shareholder litigation settlement. As disclosed in an 8-K filing earlier this month, we have now fulfilled our obligations related to this settlement, which we discussed in our last earnings call. This included intentionally accelerating into Q4 the final $25 million payment that was due in Q1.

For the full-year 2023, free cash flow was negative $57 million which includes shareholder litigation expenses of approximately $50 million.

We exited the quarter with $79 million in cash and net long-term debt of $280 million. We have additional debt capacity from a delayed-draw term loan of $8 million as well as a $50 million revolving debt facility, providing us with sufficient financial flexibility.

In terms of our outlook for 2024, we expect full year revenue of $1,190 million to $1,240 million, Center Margin of $345 to $365 million, and Adjusted EBITDA of $80 to $90 million.

Our annual guidance assumes year-over-year revenue growth driven primarily by higher visits from clinician growth combined with a low single digit increase in the total revenue per visit. Otherwise, we are assuming generally consistent operational performance year-over-year.

Our guidance also contemplates a revenue split of roughly 50/50 in the first and second half of the year due to seasonality. Regarding earnings, as compared to 2023, where they were weighted to the second half, we expect this year's earnings to be more balanced throughout the year. This is due to the timing of investments and variation in rates which are the result of payor rate changes and other mix components like geography and services.

For the first quarter, we expect revenue of $287 to $307 million, Center Margin of $81 to $93 million, and Adjusted EBITDA of $17 to $23 million.

Additionally, we expect stock-based compensation of approximately $80 to $95 million in 2024, including approximately $20 to $25 million from new 2024 grants.

Consistent with our prior messaging on pausing M&A, we are not planning to pursue any acquisitions in 2024.

I am excited to announce that we expect to achieve a company milestone by generating positive free cash flow for full year 2024. This will be driven by improved profitability and lower capital expenditures as we continue to strategically moderate the opening of de novo centers.

We expect leverage to come down significantly this year and anticipate net leverage to be below 2.5x by the end of the year. We continue to have sufficient financial capacity to run the business, and we do not intend to raise additional debt or equity in 2024.

Related to strategic initiatives, in 2023 we recognized a total of approximately $5.5 million of costs for the HRIS and credentialing and onboarding platform. Of this, $3 million were recognized as G&A expenses with the remainder in capex. As Ken stated, for the EHR, we are focused on improving our existing platform and related processes in 2024, and therefore will not incur any costs in the current year.

In closing, we are pleased with the progress we made in 2023, and we are confident as we look ahead to 2024. Now, I'll turn it over to Danish to share the work done in 2023 and the priority areas for 2024 that will position us to achieve our commitments.

Danish Qureshi, President & COO

Thanks, Dave.

We continue to align our teams around two growth priorities: net clinician adds and clinician productivity.

We grew by 227 net clinician adds in the fourth quarter and 1,014 for the full year, bringing our total clinicians to 6,645, an increase of 18% year-over-year. Importantly, our growth in Q4 remained 100% organic for the third consecutive quarter. Our clinician value proposition remains strong, and we are proud of our clinician recruiting and operations teams' great work in delivering clinician growth in 2023.

Turning to clinician productivity. For 2023, on a visits per average clinician basis, we saw productivity increase by 2%, driven by many of the operational actions we took throughout the year. As a reminder, productivity is a function of two components, clinician capacity, or the time clinicians give us, and utilization, our ability to fill clinician time with patients.

In 2023, we put our focus towards utilization, delivering on our core commitment to our clinicians to fill their schedules by driving operational discipline throughout the patient funnel.

At the top of the funnel, we made enhancements to our primary care referral team, organic search traffic, internal clinician referrals, and enterprise referral partnerships. These actions delivered improvements in attracting new patients above the growth of our clinician base, demonstrated by our growing waitlists for services. I will note that our cost per new patient acquisition continued to decline year-over-year and we spend a de minimis amount on paid advertising as part of our top of funnel strategy.

Second, at the middle of the funnel, in terms of converting patients to scheduled appointments, we continued to leverage our digital capabilities to improve patient matching via our online booking experience, OBIE, which we rolled out nationwide. Additionally, we enhanced the patient experience with better online clinician profiles, reduced scheduling complexity, and enhancements to our phone intake processes, which is a key area for 2024.

Finally, at the bottom of the funnel, in terms of scheduled appointments converting to completed visits, our cancellation and no-show rates have now stabilized in the 9-10% range which is a significant improvement from the previous 15% level when we set this as a focus area for improvement.

As we head into 2024, we are shifting our attention to the other side of the productivity equation, clinician capacity. We have early initiatives in place to grow overall clinician capacity, with a goal to reward and incentivize those clinicians offering full-time hours.

For example, we are using tiered benefits to provide incentives such as medical coverage and 401k match to full-time clinicians. Additionally, our recruiting team is focused on attracting clinicians who desire full-time employment. And finally, we offer equity ownership through our long-term incentive program to attract and retain our highest contributing clinicians.

In addition to improving clinician productivity, we made notable strides in other areas during the past year.

First, in terms of leadership, we reorganized and upgraded our practice operations senior leadership team. We made significant changes, streamlining the number of senior leaders, promoting top performers, and bringing in new external talent with the appropriate skillset to guide an organization of LifeStance's current and future scale.

Second, in terms of KPIs, we reoriented our operations teams around a metrics-driven approach to managing the business and instituted a new reporting suite of KPIs to bring focus, prioritization, and data-driven decision-making to the organization, while continuing to emphasize the patient and clinician experience.

Third, in terms of culture, we recentered the company around supporting local operations and clinician needs, while emphasizing belonging and connection. For example, we prioritized increased teammate engagement via social gatherings, recognition and appreciation, and participation in community volunteer events.

Fourth, in terms of cost efficiency, we completed our real estate optimization project. In total, we consolidated 82 centers in 2023, with little to no disruption to our patients and clinicians. We opened 35 de novo centers and will continue to intentionally moderate our pace of openings, with an expectation of no more than 20 de novos in 2024.

Finally, we made tangible progress in standardizing and streamlining the business, including moving to a single EHR, phone system, KPI suite, and online booking tool, as well as creating a single operating model for our regional support teams.

Looking ahead to 2024, there is no shortage of opportunities for improvement, with many new initiatives unlocked by the work done in 2023.

Delivering an amazing patient and clinician experience remains a top priority for us. I'd like to take a moment to discuss three tangible examples of how we are going to do this, while also generating operating leverage.

First, we are continuing to invest in the front office of our centers, focusing our resources on those areas of support that most directly impact the experience of our patients and clinicians. We are increasing our center staffing levels over 25% by year end and redesigning our processes to better support our patients, clinicians, and administrative support teams.

Second, we are making improvements for new patients booking by the phone. We are rolling out a new phone booking tool that leverages the matching capabilities of OBIE, our online booking tool. This will further enhance the patient matching experience while significantly reducing complexity and increasing the speed of scheduling over the phone for our intake team.

Third, we are piloting a new digital patient check-in tool that will allow us to collect and verify patient information upfront, as well as allow patients to pay their balances more easily. This will reduce stress for our patients and manual complexity for our operations and billing teams.

We are doing all three of these things while also meeting our commitments to margin expansion in 2024, demonstrating that delivering improved patient and clinician experiences, while also delivering improved operating leverage, can be accomplished simultaneously.

I am proud of what our teams have accomplished over the past year and am equally excited about the opportunities in front of us in 2024 and beyond. I am also particularly proud of the strength of the leadership bench that we have built, which delivered on our commitments for the full year 2023 and will be instrumental in leading the long-term, profitable growth of the business.

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

Ken Burdick, Chief Executive Officer

Thanks, Danish.

In closing, I am encouraged by the progress made in 2023. We remain focused on operational improvements, profitable growth, and disciplined capital deployment. Our 2024 guidance reflects the strong positive momentum of the organization, and we look forward to continuing to invest in the patient and clinician experience while at the same time delivering margin expansion. In particular, I am thrilled that we expect to achieve the important milestone of positive free cash flow for 2024.

Along with Dave and Danish, I offer my thanks and appreciation to our 9,500 colleagues who demonstrate their dedication to our vision, mission and values in the work they do every day. It is due to their collective efforts that we have made significant strides toward realizing LifeStance's potential.