FINAL TRANSCRIPT

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CORPORATE PARTICIPANTS

Mary Morrisey Gabriel
Gentiva Health Services - SVP & Chief Sales Officer

Ron Malone
Gentiva Health Services - CEO

John Potapchuk
Gentiva Health Services - CFO

Al Perry
Gentiva Health Services - President and COO

CONFERENCE CALL PARTICIPANTS

Matt Ripperger
Smith Barney - Analyst

John Ransom
Raymond James - Analyst

Sheryl Skolnick
Fulcrum Global Partners - Analyst

Arthur Henderson
Jeffries & Company - Analyst

Tony Campbell
David Knott Partners - Analyst

Eric Gommel
Legg Mason - Analyst

PRESENTATION

Operator

Good morning. Welcome to Gentiva second quarter 2004 earnings conference call. [OPERATOR INSTRUCTIONS]. Here, with our opening remarks is Gentiva Health Services' Senior Vice President and Chief Sales Officer, Miss Mary Morrisey-Gabriel. Please go ahead, ma'am.

Mary Morrisey Gabriel - *Gentiva Health Services - SVP & Chief Sales Officer*

Thank you for joining us this morning. I'm Mary Morrisey Gabriel, Senior Vice President and Chief Sales Officer at Gentiva Health Services, and this is Gentiva's second quarter 2004 earnings call. We hope that each of you has had a chance to review the Company's second quarter earnings report, which we released after close of market yesterday.

In a moment, I will turn the call over to our Company's Chief Executive Officer, Ron Malone, for remarks on Gentiva's performance during the second quarter, and to John Potapchuk, our Chief Financial Officer, for a closer look at our financial results and outlook.

Also joining us for the call and the question-and-answer period are Al Perry, Gentiva's President and Chief Operating Officer, and other key executives.

Let me remind participants on this morning's call that comments made by Gentiva executives and associates, other than historical information, should be considered forward-looking, and are subject to various risk factors and uncertainties. For example, our strategies and operations involving risks of competition, changing market conditions, changes in laws and regulations affecting our industry, and numerous other factors discussed in our second quarter earnings release and in our filings with the Securities and Exchange Commission.

Accordingly, actual results may differ materially from those anticipated in any forward-looking projections or comments on this call today. Please refer to the forward-looking statement in our news release issued last evening, as well as similar language in our most recent 10-K.

We also are operating under the Securities and Exchange Commission's Regulation FD. Our call this morning, and comments within it, will be consistent with our obligations under these SEC regulations. As such, we strongly encourage participants on this call with questions to present them during today's question and answer period, because under Regulation FD, we have certain limitations on comments that can be made in individual inquiries.

We also are mindful of Securities and Exchange Commission Regulation G. Regulation G requires public companies that disclose or release non-GAAP financial measures to include in that release or disclosure a presentation of the most directly comparable GAAP financial measures, and a reconciliation of the disclosed non-GAAP financial measure, to the most directly comparable GAAP financial measure. Because of this, we will not discuss non-GAAP financial measures on this call, other than what is set forth in our earnings release.

I'd also like to mention that Gentiva continues to have a policy of being open and responsive to inquiries related to our Company. In the Investor Relations section of our Company Web site, Gentiva.com, you will find our press releases, our investor presentations and many of our SEC filings. In accordance with Regulation G, a transcript of this call will be posted to the website and available for the next 12 months. Additionally, you may access our earnings call replay for the next 30 days. We appreciate your continued interest in Gentiva Health Services.

Now let me turn the call over to Gentiva's Chief Executive Officer, Ron Malone, for comments on the Company's second quarter 2004 performance.

Ron Malone - *Gentiva Health Services - CEO*

Thanks, Mary. Good morning, everyone, and thanks for joining us. We reported solid results for the second quarter, especially in Medicare and in our non-CIGNA commercial insurance business. These results are consistent with the strategies we've discussed on past calls.

Here are some of the highlights of the quarter. Our net income, as reported, was $6 million, or 22 cents per diluted share, compared to $5.2 million or 19 cents per diluted share, in the second quarter of 2003. As we explained in the news release, the 2004 figure is based on a tax rate of 39%, while the 2003 number is based on a tax rate of 7.8%.

Net revenues, as reported, were $208.2 million, nearly even with the $208.4 million reported for the same period last year. Revenues were essentially flat for the quarter, due to a 12.8% revenue decline from the CIGNA Healthcare contract, the causes of which we discussed on our last call. However, total company revenue for the second quarter was up 7.4%, excluding CIGNA revenue.

Gross margins increased more than 4 percentage points. We have continued to leverage our sales, operational and clinical strategies and, as a result, achieved a 55% increase in operating income. In the second quarter, we generated positive cash flow from operating activities of over $6.4 million. Our balance sheet remains strong, with more than $111 million in cash, cash equivalents and restricted cash at the end of the quarter.

Late in the quarter, we began implementation of our new five-year CareCentrix® contract with TriWest Healthcare Alliance.

On May 26, we announced that our Board of Directors had authorized a new program for the repurchase of up to a million additional shares of our common stock. And as we indicated in our earnings release, there were several items affecting comparisons between the second quarter and six-month results for 2004 and 2003. For that reason, we have included information on net income as adjusted in the release, and John will discuss that in more detail.

I'm pleased to report that our Medicare revenues increased 28.3% in the second quarter of 2004 versus the same period last year. This represents our fourth consecutive quarter of double-digit Medicare growth. Reasons for this growth include: operational improvements, allowing us to turn referrals into a 13% increase in Medicare admissions during the second quarter; the increased productivity and maturity of our expanded sales force; higher reimbursement rates in effect this year versus last; and the contribution of our growing specialty programs. In fact, nearly half of the second quarter Medicare increase came from our specialty programs. Those include Orthopedic Services, which is our largest specialty program, and Safe Strides, for people with balance issues, which has now launched in several locations.

We are also currently in the process of moving our cardiopulmonary specialty program from pilot to launch, and as many of you know, our specialty services are complemented by our Rehab Without Walls® program for patients with traumatic and acquired brain injuries. Also contributing to our growth was the successful rollout of increased performance reporting through our Gentiva Performance Suite application, as well as additional training for our clinicians.

Turning to our commercial insurance payers, we saw revenue for our commercial insurance and other category decrease 6.8% in the second quarter of 2004 versus the same period of 2003. The decrease came from the CIGNA revenue decline that I mentioned earlier. However, we also achieved an increase in non-CIGNA commercial insurance revenues that partially offset the decrease in CIGNA business during the quarter. CIGNA, which is our largest customer, represented approximately 32% of Gentiva's total net revenues in the second quarter of 2004. This compares to 37% in the second quarter of last year.

Our pipeline of new managed care business remains active, and we are pursuing new opportunities to apply our unique CareCentrix model. In the second quarter, for example, we announced the TriWest agreement to demonstrate how the CareCentrix model can be used to manage homecare for a vast and diverse military population and their families covering 21 states.

On the last call, we discussed the reconfiguration of our provider network and provider management models, and those changes are performing to our expectations. This initiative has helped give CareCentrix an even stronger differentiation in the marketplace.

Turning to our third payer group, Medicaid and Other Government, revenue in this category declined by 8.6% in the second quarter of 2004 versus the same period last year. This is due to a reduction in the Company's participation in certain low-margin, hourly Medicaid and state and county programs. However, in some states, we are already seeing initiatives to shift more resources to homecare, so we continue to evaluate opportunities as they present themselves in this dynamic environment.

Speaking of government programs, the Medicare reimbursement environment appears to be stable for next year. On May 28, the Center for Medicare and Medicaid Services issued a proposed rule announcing new changes affecting the prospective payment system, including a 2.5% market basket inflation increase for reimbursements beginning January 1.

We continue to work in Washington and in the states to educate legislators as to the cost advantages of homecare over institutional care, as well as the fact that most patients prefer to receive their healthcare at home. We are now working with members of Congress to increase their focus on homecare as a way to leverage the efficiency of federal healthcare spending.

Turning to our recruitment and retention initiatives, we have continued to work on reducing turnover among all associates, with a special focus on our caregivers and we are making good progress in this area. At the same time, the number of full-time caregivers increased by 25% in the second quarter of 2004 compared to the same period last year.

In the third quarter, we will be introducing a new, more flexible and affordable medical and insurance benefits program for our caregivers who are paid per visit or per hour. These plans offer incentives for them to make a stronger commitment to Gentiva and to consider full-time opportunities. We have implemented our Hiring and Promoting for Excellence programs we mentioned last quarter. We are attracting top candidates to Gentiva, and are working hard to build a high performance culture for retaining the very best people.

To sum up, I believe our second quarter results and our business strategies are on track for another solid year and we are continuing to make progress in achieving our long-term goals. With that said, I'd like to turn the call over to our CFO, John Potapchuk, for a discussion of our financial performance. John?

John Potapchuk - *Gentiva Health Services - CFO*

Thanks, Ron, and welcome, everyone. Before I discuss Gentiva's financial results and our 2004 outlook in more detail, I'd like to review a number of items that affect our presentation format and the comparability of our statements of income for the 2004 and 2003 second quarter and six-month periods.

The first is a pre-tax gain of $946,000 recorded in the second quarter of 2004, relating to the sale of our 19.9% interest in a Canada-based company to whom we sold our Canadian operations in November of 2000. We received a $4.1 million payment early in the second quarter upon closing this transaction.

The second is our first quarter 2004 settlement of an appeal to the U.S. Provider Reimbursement Review Board, or PRRB, related to the methodology used for determining Medicare reimbursements in our 1997 cost reports. We received approximately $9 million from this settlement and this amount was recorded as net revenues and pre-tax income in the first quarter of 2004. By the way, the agreed-upon methodology will also be applied to cost reports covering the years 1998, 1999 and 2000. We anticipate that the reopening of the 1998 cost reports will be completed by the end of this year. Cost reports for the years 1999 and 2000 are not expected to be reopened and completed before 2005. As we said on our last call, it is likely that future recoveries of funds for any of these years will be significantly less than the 1997 settlement.

The third item relates to our revenue adjustment of $1 million in the first quarter of 2004, which represented Gentiva's estimated repayment to Medicare in response to its previously announced plans to recover certain payments made to homecare companies since October 2000. We discussed this item in detail on the last call as well.

And finally, a significant item affecting comparability involved the tax rates for the second quarter and first six months of 2003, which were 7.8% and 10.1%, respectively. These rates were substantially lower than the statutory rate, due to the reversal of a portion of a valuation allowance relating to the realization of tax benefits associated with net operating loss carry-forwards and other net deferred tax assets. By comparison, our effective tax rate for reporting purposes was approximately 39% in the second quarter and first six months of fiscal 2004.

Because of these four items, we also disclosed Net income - as adjusted in our earnings release, and reconciled such amounts to the reported GAAP presentation. We believe the as-adjusted presentation is useful to investors, since it reflects the Company's operating performance in a consistent manner, using a normalized tax rate for all periods and excluding the special items that I just mentioned.

As Ron indicated, we have continued to achieve strong double-digit Medicare revenue growth. Part of the recent Medicare growth was due to a market basket rate increase that became effective for patients on service on or after October 1 of 2003. This increase was adjusted from 3.3% to 2.5% for open episodes of care on or after April 1, 2004. Since the beginning of April, we have also been receiving a 5% rural add-on for certain Medicare homecare services. These two reimbursement changes had a negligible effect on second quarter results.

In the commercial insurance and other category, the CIGNA revenue decline has been caused by a previously announced reduction in CIGNA's enrolled members in 2004 and lower revenue, as well as related costs, resulting from improvements in the delivery model of certain of our products and services.

We continue to make progress on balancing our payer mix. Excluding the special items, the changes are as follows. Medicare represented 26.2% of our total net revenues in the first six months of fiscal 2004 and this was up 5.6 percentage points from the first six months of 2003. The Commercial Insurance and Other payer category represented 54.9% of total net revenues, a decrease of 3.8 percentage points from the first half of 2003.

And Medicaid and Other Government payers represented 18.9% of total net revenues, a decrease of 1.8 percentage points from the first six months of last year. Of course, what's even more important than the percentages is our ability to focus on growing our targeted revenue sources.

Turning to other financial measures, our gross profit in the second quarter of 2004 was approximately $8.7 million higher than the corresponding period of 2003. As a percentage of net revenues, gross profit margins increased 4.2 percentage points, from 33.4% in the second quarter of 2003 to 37.6% in the second quarter of 2004. About half of the gross margin percentage increase came from a favorable change in our business mix, in which the volume growth of Medicare business more than offset the anticipated revenue loss in certain low-margin Medicaid and local government programs, as well as in the CIGNA business.

The balance of the gross margin percentage increase came from improved rates in both Medicare and managed care contracts, reduced workers' compensation expenses, and the growing of our specialty programs.

Selling, general and administrative expenses, including depreciation and amortization, increased $5.6 million in the second quarter of 2004 and $10.9 million for the first six months of the year, compared to the same periods in 2003. About one-third of these increases related to field operating and administrative costs to service incremental net revenues, including revenues from our specialty programs.

The remaining SG&A expense increase -- increases resulted from higher sales and clinical care coordination expenses, as well as incremental costs associated with IT and strategic initiatives, costs associated with the reconfiguration of our CareCentrix network of HME providers, and various other items.

Our pre-tax income as a percentage of net revenues was 4.7% in the second quarter of 2004, including half a percent related to the gain from the sale of the Canadian investment. This compares to 2.7% in the second quarter of 2003. For the first six months of 2004, the pre-tax margin, excluding all special items, was 3.9% versus 2.8% for the comparable 2003 period.

Overall, we continue to be pleased with the strength of the Company's balance sheet. Net accounts receivable declined by over $4 million from the end of the first quarter and our days sales outstanding at June 27, 2004, was 58 days, a decline of one day from both the end of the first quarter and year-end 2003. At the end of the second quarter, cash, cash equivalents, restricted cash and short-term investments were $111 million.

Since May 2003, we have continued to use some of our cash for repurchases of common stocks under three programs authorizing the repurchase of up to 3.5 million shares. As Ron indicated in the news release, we repurchased 587,000 shares in the second quarter of 2004. This was done at a cost of $8.9

million, or an average cost per share of $15.12. From May of last year, 2003, through the first half of this year, we have repurchased more than 2.4 million shares in the open market at a cost of over $29 million, or an average cost of about $11.90 per share. I would also like to note that since the end of the second quarter through yesterday, July 28, the Company repurchased an additional 500,000 shares.

We have also revised the key elements of our 2004 financial outlook to reflect strong first-half operating performance, the reduction in diluted shares from the stock repurchases and the anticipated lower demand for homecare services that is normal for the industry during the third quarter. Excluding 2004 special items, our full-year earnings outlook has been raised to a range between 64 and 67 cents per diluted share versus the prior 57 to 63 cents. Our revenue outlook has been changed to $840 to $850 million. The former range was $835 to $850 million.

We can also clarify or reaffirm certain other 2004 financial targets that we presented earlier this year. We now -- first of all, we now anticipate that our net revenue growth, excluding CIGNA revenue, will be in the range of approximately 9% to 12% for the year, versus the prior range of 8 to 12% growth. Our current outlook reflects diluted shares of 26.8 million, as compared to our earlier target of 27.2 million shares.

The target for capital expenditures has been changed to a range between $9 million and $12 million versus the prior range of $12 to $13.5 million. Depreciation expense should range between $7.5 and $8 million versus the previous range of $8 million to $9 million. Finally, we reaffirm our target of cash flow from operating activities, excluding special items, to be between $25 million and $30 million.

That completes our financial discussion. Now, I'd like to turn the call back to Ron. Ron?

Ron Malone - *Gentiva Health Services - CEO*

Thanks John. That concludes our introductory remarks, and we'd just love take your question now.

QUESTIONS AND ANSWERS

Operator

[OPERATOR INSTRUCTIONS] Representing Smith Barney, we first go to the line of Matt Ripperger.

Matt Ripperger - *Smith Barney - Analyst*

Hi. Thanks very much. Just two questions. First of all, I wanted to just clarify on your revenue guidance. Before you were saying it was in the 835 to 850 range. Now you're at 840 to 850. I believe before you were providing that guidance before the announcement of the TriWest contract. And I just wanted to see if you could clarify, you know, what the incremental impact is from the TriWest contract, why that wasn't more of a significant delta in terms of your revenue guidance from before to now, and then maybe if you could give an update in terms of how that's rolling out.

Ron Malone - *Gentiva Health Services - CEO*

Matt, this is Ron. Good morning. First of all, our initial guidance for the year included a projection of new revenue acquired and implemented during the year, being mindful of what we had projected as a loss of revenue from the CIGNA contract. So we were -- we anticipated, given the status of our pipeline, being able to bring in and implement new revenue during the year.

As it relates to TriWest specifically, we are now in the second phase of our three-phase implementation, bringing on our second set of states. It is on track to our satisfaction. We believe we will have the initial implementation complete before the end of this year. We will see revenues through -- you know, through the end of this year from that contract. John, do you want to add anything?

John Potapchuk - *Gentiva Health Services - CFO*

I'd also just add when you talk about the guidance, I might refer you back to even last year, 2003, when I think we reported that, included in our revenue of $814 million, was about 3% from new contracts that were signed during the past year. So as a result, as we put together our guidance, there is some anticipation of new contracts and TriWest, you know, just brings some of that to fruition.

Matt Ripperger - *Smith Barney - Analyst*

You know, as we look at your three different payer segments going forward, you know, after you anniversary the effect of the CIGNA contract, now how should we look at the sustainable revenue growth for your Medicare business versus your CareCentrix business versus your Medicaid business?

Ron Malone - *Gentiva Health Services - CEO*

Yeah. I think I understood your question as to how you should view the – the various growth rates once you anniversary the judgments in the CIGNA contract. We will -- based upon the environment we're in today, our understanding of our capabilities, the traction we're gaining with hiring new caregivers, including the full-time caregivers -- we will, at the branch level, continue to build our Medicare practice. We will watch carefully the developments in the various state programs that are reimbursed by Medicaid, and we will, you know, use the flexibility we have to move into those programs where it makes sense for us. And we believe that the -- we have a good, active pipeline on the managed care contract side, and we would expect to constantly be evaluating the profitability of those accounts, making adjustments where we need to, but we're certainly hopeful of continuing to grow that.

I would point out though, that as you look at the percent that those various payers make of our total mix, that could change from time to time because of the size of some of the managed care opportunities we have. But frankly, right now we're very pleased with the progress we're making on all three of those fronts and really managing a change in payer mix out in the system.

Matt Ripperger - *Smith Barney - Analyst*

Great. Thanks very much.

Operator

And thank you, sir. And next, representing Raymond James, we go to the line of John Ransom.

John Ransom - *Raymond James - Analyst*

I can think --

Operator

I may beg your pardon Mr. Ransom, your line is breaking up.

John Ransom - *Raymond James - Analyst*

Can you hear me?

Operator

Yes. Please, go ahead.

John Ransom - *Raymond James - Analyst*

Just a couple of questions. Ron, could you help us on your commercial (inaudible) what standard rate per visit looks like and could you compare that to kind of your Medicare rate per visit?

Ron Malone - *Gentiva Health Services - CEO*

And did you have another question, John, we can get right now?

John Ransom - *Raymond James - Analyst*

Sure. And secondly, I guess, yeah, I'm surprised that that cash is still kind of sitting there on your balance sheet, and you know, relative to buying your own company stock at, you know, roughly 8 times EBITDA, I didn't know what the acquisition environment might look like out there at maybe lesser EBITDA multiples.

Ron Malone - *Gentiva Health Services - CEO*

Okay. Thank you very much, John. Good to have you on the call. First of all, as it relates to rates per visit, it's really in our minds comparing apples and oranges because of the extraordinary difference in the demands of participation in the Medicare program versus, in many cases, the more streamlined requirements associated with managed care. For instance, you may recall that the modernization act of last year suspended the need to process OASIS paperwork on non-Medicare, non-Medicaid patients. Those kinds of differences make a -- you know, can make a marked difference in the operating costs.

We've said for, I know several years, that Medicare is generally the highest gross margin service that we address, aside from perhaps some hourly business here and there, as a general category, the highest, but it also has the highest cost of participation as well. So the need to complete OASIS on assessment and on discharge and the intense documentation and review requirements we have, I think just renders it a very difficult comparison for us.

As it relates to our cash balance, you know, we feel pressure, John, to do a lot of things right here. We feel pressure to hire and retain the best people to continue a good growth rate in the Company, a balance of payer mix and a good environment. But I think most of all, I feel pressure that we would make the right decisions so that Gentiva is successful in growing the enterprise for the very long term. So we do not feel pressured to make any short term or short-sighted decisions.

That said, I think that the -- we said last time and I think we would reiterate that we're giving more time and attention and thoughtful consideration to the acquisition opportunities out there. We don't take for granted the execution and integration of any of those opportunities. So we're -- I think, again, the best thing probably for me to say is we're simply thoughtful in this area and take a very measured approach. Thank you, John.

Operator

And thank you Mr. Ransom and next, representing Fulcrum Global Partners, we go to the line of Sheryl Skolnick. Please go ahead.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Good morning and please don't count this as a question. I apologize. I miscalculated your cash flow number in the quarter and figured that you hadn't bought stock, but you did. So I apologize for me making that mistake. I compared it to the December 12, '03, spend on stock instead of the first quarter, in the note that I put out this morning.

So having said that, my question then is -- the first one is, it sounds like with the shares you've repurchased this quarter, you are close to the million shares already that was being reauthorized? Is that right?

Ron Malone - *Gentiva Health Services - CEO*

We are about halfway there, Sheryl.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Okay, so the 587 was done on the last authorization.

Ron Malone - *Gentiva Health Services - CEO*

Well, yes, for the most part of it.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Okay. So you still have a little bit more room there. And so my second question, I guess, is the one with more meat, and that is this. I'm still struggling with your revenue guidance because quite frankly, with the flat revenues this quarter, I'm sort of hard pressed to see how you're going to make up for the CIGNA revenues with the TriWest contract and then some for the balance of the year because it seems like your Medicare revenues are tracking very nicely at somewhere around $55-$56 million.

And as the year goes on, your comp gets tougher because you had double-digit unit growth of 17%, I think, in the fourth quarter, and clearly, you experienced something similar to that in the first quarter, if not better, and something similar this quarter. So if I assume that that's the case, that you still get some growth there because you've increased FTEs and you're increasing your penetration of the potential referrals there, I'd still have trouble figuring out how it is you're not only going to get beyond last year's kind of net revenues by a very significant amount to, say, $825 million, but then now you're telling us, if I heard you correctly on the revenue line, you're now at 840 to 850. So you've tightened up that range, and I guess I'm just not understanding that now.

John Potapchuk - *Gentiva Health Services - CFO*

Let me just mention a couple of things, Sheryl, to see if hopefully we can clear that up a little bit. We, on the Medicare side, while you indicate that, you know, the comps get more difficult, I mean, we have four quarters in a row now of double-digit increases in admissions. Right now, included in our guidance is certainly for the near term through the end of this year, but continue to grow at a double-digit basis on admission. So that's assumption number one.

The other thing I'll mention and I think on an earlier call I may have mentioned this and I apologize for confusing the analyst, but once every five or six years, we have a 53rd week because our year-end is the Sunday closest to December 31. That occurs this year. Our year-end is January 2 and the fourth quarter has an extra week in it, and that certainly is built into the numbers also.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Okay. So I'll have to figure out how much seven days revenue gives you, but I mean, can I just go back and clarify this because you're telling me in the fourth quarter on top of 20+%, you know, 17% unit growth in Medicare admissions last year, that you can do something comparable to that this year? I mean, that's my problem is that you've got -- you have spectacular growth and double-digit might not be 20%; it might be 10.

John Potapchuk - *Gentiva Health Services - CFO*

Right.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

So, you know, that I might buy and even if -- what I'm saying to you is even if I give you some credit for that -- I'll have to go back and do the math -- I guess I'm just concerned that, you know, the expectations for back half revenues seem pretty robust. And I don't know if it's because you have so many more FTEs or what it is exactly that -- but I feel like I need a little more comfort on that, and I'll figure out what a week's worth of revenue is worth.

John Potapchuk - *Gentiva Health Services - CFO*

I think, Sheryl, the other thing I might just point is that as Ron mentioned in the opening remarks, that our pipeline in new managed care business remains very active, and you know, there's potential certainly for some additional contracts.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Okay. So is it fair to say you have about $15-$16 million of revenue a week?

John Potapchuk - *Gentiva Health Services - CFO*

Sixteen. In the second quarter, we averaged 16 a week.

Operator

And representing Jefferies & Company, our next question comes from the line of Arthur Henderson.

Arthur Henderson - *Jeffries & Company - Analyst*

Hey, guys, how you doin'? Let me understand something that you guys said earlier. Your Medicare admission -- or your Medicare growth was 28%. Did I hear you say correctly that that was nearly all volume and just a little bit of price? Can you detail that for me?

Ron Malone - *Gentiva Health Services - CEO*

Arthur, how are you doing? This is John.

Arthur Henderson - *Jeffries & Company - Analyst*

Good.

John Potapchuk - *Gentiva Health Services - CFO*

What we said was that the volume of admissions was up 13%. What -- the rate on a net basis increased 2.5% and then certainly, the difference is the mix of the type of patients we're servicing within the Medicare area.

Arthur Henderson - *Jeffries & Company - Analyst*

Well, because you're --

John Potapchuk - *Gentiva Health Services - CFO*

What I mean by that is close to half of the Medicare growth involves our specialty programs, orthopedic and Safe Strides and certainly, the severity of that and the revenue on a per-episode basis is greater than, you know, what it's been in the past. So that certainly contributes to that increase also.

Arthur Henderson - *Jeffries & Company - Analyst*

Okay. So 13%, just on a volume basis, plus the fact that you're getting a more favorable mix in terms of price, based upon your specialty programs?

Ron Malone - *Gentiva Health Services - CEO*

That is correct.

Arthur Henderson - *Jeffries & Company - Analyst*

Okay. My second question is, is that on the -- I assume that you look at a lot of acquisitions and that a lot of acquisitions are brought to you in some manner or another. My question is, you made a recent -- or you made an acquisition a while back in Houston and it was small, and you focused on integration issues. What's preventing you from making a move on one of the acquisitions that you may look at today? I mean, is it just you're really concerned about integration, or are the quality of the acquisitions that are coming to you poor? I mean, what are the reasons?

Ron Malone - *Gentiva Health Services - CEO*

Art, this is Ron. Good morning. I think that the quick, smart answer is yes. All of those things in one form or the other may impact the way we would look at any particular opportunity out there. Let me just mention a couple of things that we look at very closely. One, we look at very closely -- first of all, at the culture of the company including the aspect of -- you know, compliance and how they have actually performed in a Medicare-Medicaid environment. So we're very concerned that any group of people that were to join our Company, you know, sustain that relationship for a longer period of time. We are concerned also with the integration associated with companies with a high amount of overlap in the markets that we already serve. You know, our history and some of what we know about transactions would indicate that that's an area we should be mindful of as we look at these opportunities.

We also look at the mix of business. We have said that we have less interest in some of the Medicaid state and county programs that involve services of lesser skill. We're more focused in the Medicare area, and then within Medicare, we also, of course, are mindful of these price expectations out there in the market right now. So I think all of those things weigh into what we look at, or we look at it -- as we look at a particular opportunity.

Arthur Henderson - *Jeffries & Company - Analyst*

Are there some acquisitions out there -- maybe they're not in the market to sell their company yet, but are there some that you have identified that you would like to move on, given the opportunity?

Ron Malone - *Gentiva Health Services - CEO*

I think we just -- you know, our policy is not to comment on that activity beyond saying earlier that, you know, we're spending more time and energy in this area, and we certainly, you know, have been mindful that we have the resources.

Arthur Henderson - *Jeffries & Company - Analyst*

Okay. Thanks a lot.

Operator

And representing David Knott Partners, our next question comes from the line of Tony Campbell. Please go ahead.

Tony Campbell - *David Knott Partners - Analyst*

Good morning, gentlemen. I'm wondering if you guys, because I guess there's concern about revenue growth, could you give us some more detail on some of these new business opportunities and potentially sort of give us some idea of how big, you know, the size of the markets that they face and how big they could be for you?

Ron Malone - *Gentiva Health Services - CEO*

Well, let me take TriWest as an example. We had announced that that was covering over 2 million lives. So, you know, that in and of itself, given the -- you know, we had also said it is a contract to provide comprehensive homecare services from skill care to durable medical equipment, oxygen and infusion therapies. So that in and of itself is a large revenue opportunity for us, and as I mentioned earlier, Tony, we're implementing it, I think, right on track. It often takes time to really -- you know, this is enormous change. In fact, it's considerable change for our client in this situation because they're bringing on a number of new lives themselves. So our expectation is it would take a while to build that business, but we believe we have the foundation for a very good partnership there. This is also a business that we usually do our best to absorb internally, so that we're filling as much of the skilled nursing needs in our branches as we're able to. That will also take a little bit of time to ramp up.

I think in general I would be mindful on a day where we're standing very tall, we might -- we still probably have less than 3% of the opportunity in the homecare market, and we wouldn't necessarily, as we said before, restrict our future interests just to home -- you know, just to traditional homecare either. I think the specialty services that we've mentioned, where we have the orthopedic out now. We are very pleased with the Medicare growth rate. The orthopedic growth rate is considerably higher than the Medicare growth rate. So we believe that the strategy of really dividing our Medicare-certified branches into essentially programs and more focused practice areas with practice leaders is a driver of both higher clinical quality, which we think makes -- is going to make a tremendous difference in the long term, as well as simply a higher growth rate because we're able to focus on specific positions that are themselves focused in a given disease state.

We have cardiopulmonary. We have Safe Strides up and running, and in the rollout, we have about four locations open now but anticipate opening up to ten by the end of this year. We have the cardiopulmonary program through the pilot ready to launch. We have a couple of other programs in the wings that we're working on that we'll tell you about later. And all this means to me, add together, that over time, we have a tremendous opportunity to grow and to penetrate this market.

And frankly, I'm very pleased with the progress we're making, particularly given that we have been through a protracted rebalancing of our portfolio where we're, you know, getting the amount of less desirable business down. We're adding to the better part of the mix and that involves not only a mindful management process around the contracts, but it means also a transition in the type of caregivers that we have on board at any given time. So all that taken into account, I'm quite pleased with the progress we're making and have considerable confidence in where we're going.

Tony Campbell - *David Knott Partners - Analyst*

Well, could I get you to go on the record that, you know, assuming that you execute as you have in the past, that we might be able to see an acceleration in your growth some time in the next couple of years because of these new specialties?

Ron Malone - *Gentiva Health Services - CEO*

We -- I -- the whole ratio -- we haven't gone yet into the period of trying to give an outlook for the next year or two years, for that matter. We certainly are working very hard, both on the operation side at the branch level, in our CareCentrix call centers, as well as in our entire sales team to do just what you indicate. It's a high priority of ours. We are only pleased within the context of never being pleased and we think that there is considerable opportunity. We think that we have both the talent and the resources to withstand any changes out there in the environment, and probably if anything, to actually benefit from some changes. So I have a considerable amount of confidence, short of giving you an outlook, Tony.

Tony Campbell - *David Knott Partners - Analyst*

Okay. And then finally, if I might. I presume that you plan to complete your authorization and then reauthorize and go forward and do it again, potentially?

Ron Malone - *Gentiva Health Services - CEO*

Well, it is certainly up to the Board to make that decision. We have said before we have a considerable amount of confidence in the Company and so, we'll certainly keep you informed as we make those decisions.

Tony Campbell - *David Knott Partners - Analyst*

All right, good luck.

John Potapchuk - *Gentiva Health Services - CFO*

Thank you very much, Tony.

Operator

And thank you, Mr. Campbell. [OPERATOR INSTRUCTIONS] And representing Legg Mason, we next go to the line of Eric Gommel. Please go ahead.

Eric Gommel - *Legg Mason - Analyst*

Yes, thanks. I just really had one question. You know, we're seeing both in the long term acute care hospital space and the inpatient rehab space coming under greater scrutiny from CMS, limiting admissions, you know, greater regulations, and really, we believe it's a general trend towards utilizing the lowest cost provider. Is there potential for the homecare space to handle some of this higher acuity population? I'd be interested to get your thoughts on how you look at homecare as a potential substitute versus nursing homes, LTACs and IRFs?

Ron Malone - *Gentiva Health Services - CEO*

Well, we believe -- thank you for the question, Eric. We believe strongly and we believe that -- we think our beliefs are underpinned by the history of the past few years, that there's already been a trend to deliver more -- you know, more care to more acute and chronically ill patients in the home. We have a number of therapies that have been shifted into the home over the past few years that previously required skilled facilities of one kind or the other, and we think that there is a considerable amount of room to grow that.

Let's face it. Healthcare is an issue that is going to confront this economy and this country for a long time and we have to find ways to deliver that care more efficiently. I can't think of a better place to look than the intersection of where people are most comfortable and would like to receive the care. They'd like to recover in the home and the efficiencies brought about by the delivery of that care, I think the economic model is pretty well stated. The thing that we are looking forward to is more and more independent studies that really confirm that, so it makes it much easier for our legislators.

By the way, as it relates to regulation, I would suggest that maybe some of those other groups are just catching up. I think we are a heavily regulated industry, have been for a number of years. So I think maybe some of the others are just now catching up.

Ron Malone - *Gentiva Health Services - CEO*

Thank you, Eric.

Eric Gommel - *Legg Mason - Analyst*

Thanks.

Operator

And thank you, Mr. Gommel. And we do have a follow-up question from Matt Ripperger with Smith Barney. Please go ahead.

Matt Ripperger - *Smith Barney - Analyst*

Great. Thanks very much. Just a couple of follow-ups. First, in this most recent quarter, your SG&A costs were up about 8% year-over-year and your revenues were pretty flat, and I know you've made a pretty big investment in systems and sort of infrastructure. I just was wondering, you know, as you look forward, where will we cross that point where we'll start to get some leverage of your SG&A costs? And therefore, your revenue growth will start to materially exceed what you're increasing in your administrative cost?

John Potapchuk - *Gentiva Health Services - CFO*

Well, Matt, I think if you just look at percentages on SG&A and revenue, that's obviously a bit deceiving, given the -- you know, given the changes with CIGNA which obviously created the flat revenue. And the fact that in the first half of the year, as I mentioned in my remarks, you know, among our increases in SG&A, a portion of that related to the reconfiguration of the CareCentrix network. So some of that is behind us and I think some of that certainly, you know, you'll see some changes in the trend from that area. But of course, included in the SG&A changes, I did indicate that both IT and strategic initiative costs that we incurred, and that's certainly going to continue for the foreseeable future.

So I mean, I think as we -- you know, as we continue to grow that revenue and change that mix and certainly, you know, with CareCentrix work that we've done, you know, there's the opportunity for further leverage, but certainly, I'm pretty pleased with what happened in the second quarter here.

Matt Ripperger - *Smith Barney - Analyst*

Okay. And then the second question I had is, you know, just getting back to the latter half of this year's guidance, your revenue guidance is implying basically about $430 million in revenues in the third and fourth quarter, which is actually higher than the revenues you reported in the first half of this year. And yet your earnings guidance is implying that your third quarter will be down sequentially and your fourth quarter will be down as well from where you were in the second quarter. So am I led to believe that you're just bringing on higher revenue CareCentrix business, just lower margin?

John Potapchuk - *Gentiva Health Services - CFO*

Matt, your –

Matt Ripperger - *Smith Barney - Analyst*

Basically, your revenues in the back half of this year will be greater than the first half, that your earnings are projected to be down?

John Potapchuk - *Gentiva Health Services - CFO*

Well, of course, in the third quarter and I -- in our guidance, we talked about the anticipated seasonal decline in the third quarter, which is kind of normal in the industry. When you think about the fact that as a result of that, that revenue would be down somewhat in the third quarter, but certainly you have fixed cost components. I mean, you're not going to -- we don't have a variable cost business here. Your leverage in the third quarter relative to the first half of the year is going to be down.

The other point I'll make on that --

Matt Ripperger - *Smith Barney - Analyst*

Your revenue guidance implies that the back half of this year will be up.

John Potapchuk - *Gentiva Health Services - CFO*

Yes, exactly, but I'm focusing now quarter-by-quarter and the third quarter is a lower period, although you have the fixed costs. The fourth quarter will be higher as a result of that extra week, which I referred to earlier, but you also have those fixed costs and that extra week. See, when you think about that extra week that relate to the holiday season and while you're gaining more revenue, you're -- it -- I would say maybe not at the rate of a $16 million per week quarter, given the fact that the holidays are involved, but you do also have those fixed costs associated with that holiday week also. So all of that plays into it and I hope that helps a little bit at least.

Matt Ripperger - *Smith Barney - Analyst*

Okay. And then the last question I had is just, you mentioned that you've increased your full-time caregivers by 25%.

John Potapchuk - *Gentiva Health Services - CFO*

Correct.

Matt Ripperger - *Smith Barney - Analyst*

Can you just give us the number in terms of where you stand right now in terms of full time caregivers? And how does the underlying economics change for you when you transition from outsourcing to an unaffiliated caregiver versus bringing it in-house?

Ron Malone - *Gentiva Health Services - CEO*

Well, first of all, the number is a bit over 750. Right now, it's 769 or so right now. And I think as it relates to the economics[audio gap] is really, there's several moving parts. One is where, you know, we have, as opposed to this highly variable direct cost, we have almost fixed cost there because we have these folks on essentially a salary with incentives to over-perform beyond our minimum threshold of expectation. We also have generally a higher load for the statutory burden and the benefit that we provide that group of people. That is offset by the increased flexibility we get to take more cases, certainly a more flexible employee, generally more focused.

I think one of the really key things here is the focus on retention, the focus on making sure that the training we give results in an employee who, over time, is not only more productive, but more efficient as well. And I give you -- I don't have to go much further than just the assessment and discharge completion of the OASIS data set, compliance with our policies, the speed and accuracy with which they complete documentation, the relationship they have with the branch; really brings that person is as a full member of the team and in no -- you know, really bought into the success of the Company for the long term.

So we have seen -- and frankly, we've seen a good result from this, but it's something we've had to learn to manage over the last couple of years. And that's why we started, I think, probably two and half or so years ago, with about 200 full-time people, and as we've gained competence and understood how that to attract and retain and make productive these people, we have increased that number. We're also focused on getting those people who are more properly paid because of their lifestyle, fees or whatever, that are paid per visit or per shift to be more dedicated to us, and then from that population, we would hope more to recruit more into the completely -- you know, the complete, full-time status.

So I mean, it's a trend we would expect to continue and I'd like -- personally, I'd like to see nothing more than to see more and more of our visits completed by those that are associated with us on a full-time basis because I think it's good for us; it's good for our patients; it's good for our shareholders.

Matt Ripperger - *Smith Barney - Analyst*

Great. Thanks very much.

Operator

And thank you very much, sir. [OPERATOR INSTRUCTIONS] Ladies and gentlemen, we appreciate the interest shown in today's conference. However, with time now for one more question, our final question comes from Sheryl Skolnick, a follow-up once again from Fulcrum Global Partners. Please go ahead.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

I'm glad I got this in. I don't know if anybody said this, but you did really do a very nice job this quarter. Thank you. And despite all the complaining and grousing about your revenue number, I want to go back to two little issues here that -- to the FTEs being up 25%. I guess I'll ask the question -- there's two parts to this. One, does that give you any excess capacity? Or another way to ask that question is to say if you've increased your FTEs by 25 %, by how much does that allow you to increase your unit volumes or your revenues, what's ever an easier way to think about that?

Ron Malone - *Gentiva Health Services - CEO*

Well, in some branches it does give us the opportunity, but we're also mindful, Sheryl, of in some cases, managing out caregivers that are at the other end of the spectrum --

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Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Sure.

Ron Malone - *Gentiva Health Services - CEO*

-- that have a very casual attachment with the Company. It may take us -- you know, if you look at like the inside operations of a branch, we're sensitive to how many do calls our people -- our schedulers have to place in order to make sure that we have attained coverage. Well, in most cases, when you call on the full-time caregiver, the answer to that is one or near one, but on the other end of the spectrum, it could be four or five or six. So we really are going through a transition where we -- what we are measuring internally is, we look at the productivity of these categories, but we're looking at increasing the full-time complement, those that are working for us, let's say broadly, more than 30 or 32 hours a week, and that could be in that sort of 30 to 45 category.

We have an active effort underway to help a group of people make the decision to move from, say, under 15 hours for us to the 15 to 30 hours category and then to, in some cases, disassociate with those that might cost us more to employ than we get in benefit at the very lower end of the productivity scale. But I mean, generally, you know, a new full-time caregiver coming on board allows us to take, depending upon the type of mix, we have several more patients per week. And as you would realize certainly, that capacity is sort of -- you know, is static at a point in time. So on Thursday afternoon, we had exactly a certain amount of availability. You either use it or you don't.

That's one of the things we're also looking at, implementation of the CaseMatchSM. We're pleased with the improvements we're seeing there, the use of the CaseMatch tool because we believe we can take that finite group of people and more fully employ them or fully deploy them at any given point in time.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Okay. A related question and then a little tiny follow-up. The related question is when did you start with the -- paying for or offering the medical and other benefits to the part time employees? Was that in the second quarter?

Ron Malone - *Gentiva Health Services - CEO*

We started in, I believe, 2001, offering -- we changed again in 2003 and will change again this fall to make those, as we said, more flexible and more affordable for them. I've been really mindful of this, Sheryl, because you know, trying to really understand that group of people and what their needs are for, for instance, normal health coverage versus catastrophic coverage and the various things that will a little bit more casually attach. We also expect to have a pilot to bring in more people that are sort of in that 30 to 40 hour range as well. Those are the very valuable nurses and therapists for us. Their lifestyle needs may be such as they are almost full time, but not quite. We're going to offer them a better package and run a pilot there because we believe we can increase capacity that way as well.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

That makes a lot of sense. And then finally, since you do have managed care business, unlike some of the other public companies in this space, are you seeing any issues with collectability of co-pays for homecare services that we need to be concerned about?

John Potapchuk - *Gentiva Health Services - CFO*

Sheryl, we -- certainly, the amount of patient pay-related co-pay is increasing as our business grows, but we're collecting a fair percentage of it. We've put in a number of practices to continue to increase that percentage and right now, we're pretty pleased with that.

Ron Malone - *Gentiva Health Services - CEO*

Yes. We have completely revised our consumer invoicing, which resulted in much more clear information, much easier to pay statements. You know, we accept credit cards and it's an area that we recognize. That trend probably, John, two and a half years ago, that trend started edging up and then deployed resources around that area, so that we wouldn't because, Sheryl, as we've discussed before, we were also looking at the -- you know, just the general increase in co-insurance and co-payment. We thought that's a trend that's probably not going to do anything but accelerate, so we needed to get -- we tried to get ahead of it a couple of years ago.

John Potapchuk - *Gentiva Health Services - CFO*

Right. And in our Tampa unit, we actually have a group that is dedicated and focused on the patient paydowns.

Ron Malone - *Gentiva Health Services - CEO*

It is a consumer pay.

Sheryl Skolnick - *Fulcrum Global Partners - Analyst*

Great. Thanks so much.

John Potapchuk - *Gentiva Health Services - CFO*

Thank you very much.

Ron Malone - *Gentiva Health Services - CEO*

I would like to thank each of you for your participation this morning for your continued interest in Gentiva Health Services. We will continue to keep you informed about our progress during the year. I hope you enjoy the rest of your summer and we will speak with you again on our third quarter earnings call.

Operator

And ladies and gentleman, your host is making today's conference available for digitized replay for one week that starts at 1:30 p.m. Eastern daylight time July the 29th all the way through 11:59 p.m. August the 5th . To access AT&T executive replay service, please dial 320-365-3844 with the Conference ID of 739257 and as Mr. Malone just said that does conclude our earnings call for this quarter thank you very much for your participation as well as for using AT&T's executive teleconference service. You may now disconnect.