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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the LHC Group Fourth Quarter 2018 Earnings Conference Call. (Operator Instructions) As a reminder, this call is being recorded. I would now like to introduce your host for today's conference, Mr. Eric Elliott, Senior Vice President of Finance. Please go ahead.

Eric C. Elliott - *LHC Group, Inc. - SVP of Finance*

Thank you, Christie, and good morning, everyone. I'd like to welcome you to LHC Group's earnings conference call for the fourth quarter ended December 31, 2018. Everyone should have received a copy of our earnings release last night. I would also like to highlight that we have posted some supplemental information on the quarter, full year 2018 and our guidance for 2019 on the Quarterly Results section of our Investor Relations page. The supplemental deck, as well as a copy of the earnings release, the 10-K and ultimately a transcript of this call, when available, can be found on this page. Our supplemental deck includes all of our reconciliations and breakdown of the adjustments. We will refer to these non-GAAP measures during our call today.

In a moment, we'll have some prepared comments from Keith Myers, Chairman and Chief Executive Officer; Josh Proffitt, Chief Financial Officer; and Don Stelly, President and Chief Operating Officer.

Before we start, I would like to remind everyone that statements included in this conference call, in our press release and in our supplemental financial information may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act. These statements include, but are not limited to, comments regarding our financial results for 2019 and beyond. Actual results could differ materially from those projected in forward-looking statements because of a number of risk factors and uncertainties, which are discussed in our annual and quarterly SEC filings. LHC Group shall have no obligation to update the information provided on this call to reflect subsequent events.

Now I'm pleased to introduce the Chairman and CEO of LHC Group, Keith Myers.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Thank you, Eric, and thank you, everyone, for dialing in and participating in this morning's call.

For the last few months, we have talked a lot about how important it has been for us to take the right steps with the integration of Almost Family and how well prepared we were for that integration to ensure we remain in growth mode. Lately, you've also heard more from us on how the in-home health care industry is positioned and the broader health care landscape is changing for the better in the eyes of the government, managed care payers and joint venture partners. We also repeatedly made the correlation between industry-leading quality to organic growth and an increase in joint venture value proposition.

We have another quarter of results to back up these discussions, and our 2019 guidance now in place, we have more clear evidence that we have a valuable and sustainable business model that is built on our strengths. Our partners are speaking openly about the value we create for them. The negotiations we're having with patients are yielding improvements on rate and margin as we work with them on innovative model arrangements. And as evidenced by the recent bipartisan senate legislation, we are seen as having a critical role in delivering superior outcomes in a more cost-effective setting in post-acute care.

Let's start with our integration activity on Almost Family acquisition. At this point, we are past looking at this as 2 separate companies. We are all one family instead of 2 separate companies, quite an achievement in less than a year. We are ahead of schedule on this integration, and we achieved greater cost synergies than we had originally anticipated in 2018 and have increased our target for 2019. This will help us potentially reach $25 million to $30 million in run rate cost synergies in the back half of 2019.

I noted last quarter that we were in the transformation phase of the integration. What does that mean, exactly? A good example would be finishing off the conversion of all acquired agencies to the LHC Group instance of homecare homebase to be able to more quickly deploy our proven workflows and processes that drive continued improvement in margin and quality scores. This conversion is on track to be finished by the end of the third quarter, and you can see the effectiveness of these early efforts and the sequential improvement in margins and quality scores.

The Almost Family integration is one of several we have ongoing. We are in various stages with joint ventures we announced in 2019, including the expansion of our existing partnership with LifePoint in North Carolina and Virginia in December. We followed up an active year of acquisitions, a record $822.6 million, in fact, with the Unity Health partnership in Arkansas in late January and this week's announcement of a partnership with Geisinger and AtlantiCare in Pennsylvania and New Jersey. In each case, our ability to show these markets are very compelling value proposition backed up by national scale was a critical factor in their decision-making. We expect more of the same for M&A activity in 2019 with both large and smaller partners. Our acquisition pipeline is robust, and we continue to review 15 to 20 highly vetted transactions at any given time.

LHC has the benefit of a low-leverage balance sheet with increasing free cash flow along with the proven capabilities to quickly and fully integrate these acquisitions. It will be a major component of our growth going forward. As I noted last quarter, if we assume acquisitions will be between $100 million to $150 million each year, a number that is certainly achievable based on our past results, this free cash flow would allow us to remain under 2x leverage for the next few years.

One final note on growth before I speak to recent events on the regulatory front. I can't help but be excited about the number of organic and inorganic growth opportunities ahead of us this year and next. I look forward to sharing more of this news as the year progresses.

Now to recent events on the PDGM model, or Patient-Driven Grouping Model. There are certainly other developments that we are tracking on the regulatory front, and Bruce Greenstein and Josh had been very active as it relates to new initiatives from the government and innovative care model for payers. What everybody wants to talk about is PDGM, so let's spend some time on what's new there.

Lately in my role as Chairman of the Partnership of Quality Home Healthcare, we have been very active working with CMS and members of the U.S. Senate and House on specific legislation to modify CMS' approach to prospective behavioral assumptions. This is a united front within the industry, and I'd like to thank all of those providers, both large and small, who have actively lobbied their members of Congress and continue to do so each day. This has been a team effort throughout on the lobbying and advocacy side.

Last quarter, we talked about several bipartisan deals that have been introduced in the Senate and the House that address various aspects of the industry's concerns about assumptions CMS had made to ensure PDGM is budget-neutral as required by the Bipartisan Budget Act of 2018. In mid-February, the latest bill was proposed by several of these senators, 7 of them in fact, from both sides of the aisle, that intends to do several things: one, require Medicare to integrate rate adjustments for home care to be based on evidence and adjusting those rates only after behavioral changes that affect Medicare spending are observed. Currently, CMS is assuming behavior changes before they occur. Number two, phase in any observed behavioral changes no more than 2% per year to maintain budget neutrality; and number three, allow the homebound requirement to be waived when a Medicare Advantage plan or an innovation center program determines that provided home care improves outcomes and reduces spending.

Additionally, Senator Colin of Maine, Cardin of Maryland introduced bipartisan legislation called of the Home Health Planning Improvement Act that would allow non-physician providers such as physician assistants, nurse practitioners, clinical nurse specialists and certified nurse midwives to certify eligibility for home health services. The industry wholeheartedly supports both pieces of legislation, and we expect there will be companion bills in the House that would be modified at a similar fashion. We don't have a time frame on when or if these bills will be taken up for consideration, but the groundswell of support for the industry has never been greater. We are confident that legislation can be achieved before PDGM goes into effect in January of 2020.

We are a 24/7, 365 health care organization that never sleeps and is counted upon to always be there to meet the needs of those we are privileged to serve in communities throughout our country. I would like to thank our many clinicians and administrative support personnel who consistently exceed expectations in their respective areas of responsibility. Know that each of you is valued and appreciated for all that you do for those we serve and for your professionalism and congeniality. It is truly a privilege and an honor for me to be part of your team.

Now here's Josh to provide some color on our financial results and guidance for 2019. Josh?

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

Thank you, Keith, and good morning, everyone. Thank you all for joining our call.

As always, I like to begin my prepared remarks by saying how much I appreciate all of our clinical professionals across the country for what they do each and every day to provide high-quality care and service to the patients and family to care for. I would also like to thank our family members from Almost Family and our home office support teams who have worked tirelessly to ensure a smooth and successful transition. To you all, a very heartfelt thank you for all that you do to that makes our LHC Group family so special.

With our supplemental financial information posted on the website and providing more detail on the breakdown among sector performance, guidance and assumptions, I would like to focus my time this morning on the larger themes evident in our results and the 2019 outlook.

For the fourth quarter financial results, here are the big takeaways: The strong finish to the year in the fourth quarter pushed us to the top end of our adjusted EPS expectations for 2018 due to a strong admissions growth and solid cost management within our general and administrative expenses. We earned $1.03 per share of adjusted EPS in the fourth quarter, bringing us to $3.55 for the year. By hitting the top end of our adjusted EPS range, we were able to deliver 14.5% accretion from our previous EPS guidance range prior to our acquisition of Almost Family. We were above our target for the year with realized cost synergies achieving $13.8 million in 2018 as compared to our expected range of $8 million to $12 million. The incremental margin improvement in the business and the ability to tap this embedded growth were evident in our results as we experienced sequential and year-over-year improvement across our segments throughout the year, particularly in the fourth quarter.

Organic growth was strong in home health and hospice yet again as we maintained our industry-leading quality and patient satisfaction scores and continued to raise the scores at the Almost Family locations. The strong year gives us added confidence in our initial outlook for 2019 and the expected adjusted earnings growth of 18.3% at the midpoint of our range. More on that outlook in a moment.

Recall that our focus during 2018 has been on operational stability, but we have already shown accelerated growth year-over-year as we generate more revenue growth and capture incremental margin from improving the operations of our acquired locations. This positive trajectory sets us up well for 2019 and beyond.

Turning to Page 9 of the supplemental deck, I would note that our adjusted consolidated gross margin of 36.9% in the fourth quarter was an improvement year-over-year. Consolidated adjusted G&A expense as a percent of revenue was 26.6% in the fourth quarter, which was down from the third quarter of 27.5% and from 28.7% in the same period a year ago. Our adjusted consolidated EBITDA was 10.2%. That was up both 70 basis points sequentially and 210 basis points year-over-year.

One important point to highlight in our fourth quarter results is that as part of our strategy to optimize the portfolio, we did close 22 locations that represented a total of approximately $30 million in revenue and a contribution loss of approximately $2 million. We incurred some severance costs, lease termination fees and impairment costs related to intangibles in connection with those closures. All of these costs were accounted for in our adjustments. This was the right move for us to take to close down these unprofitable locations and put us on a great trajectory in '19. The details of those adjustments can be found on Page 10 of the supplemental deck.

This improvement across all metrics was broad-based. Pages 11 through 16 of the supplemental deck highlight the results, and Page 7 notes the key stats by segment. Turning to Page 22, we've outlined a number of our debt and liquidity metrics as well.

Adjusted free cash flow was up 108.4% to $110.2 million for the year as compared to adjusted free cash flow of $52.9 million in 2017.

DSOs improved to 45 days from 46 days in the third quarter and from 51 days in 2017 as we continue to improve our collections on managed care receivables and receivables from the Almost Family acquisition. We would expect DSOs to remain close to that range, if not slightly below in 2019.

Our balance sheet remains strong with leverage of 1.2x adjusted EBITDA at year-end. With $240 million available in our credit facility and an accordion feature that can provide an additional $200 million of capacity, we are well positioned to remain in growth mode on the acquisition front for the foreseeable future.

On Page 17 of the supplemental deck, we've outlined our guidance for 2019. At the midpoint of this range, we're expecting adjusted EPS growth of 18.3%, net service revenue growth of 16.3% and adjusted EBITDA growth of 32.7% as compared to 2018. The key assumptions are listed as well, but I'll call your attention to the cost synergies we are expecting from the A-FAM acquisition of $12 million to $17 million in 2019. Our stated guidance is based on $25 million in realized synergies, but we believe that we have the potential to reach $30 million by the end of the year. This would naturally equate to get to a quarterly run rate synergy that's higher in the second half of 2019.

There are 2 other factors to remember in our guidance, especially in terms of the expected revenue. The first is that we are expecting a 1.2% increase from the 2019 home health Medicare PPS update. The second is that 2018 included the results of the 22 locations that we closed in the fourth quarter that I referenced earlier that represented nearly $30 million of annual revenue. That revenue is not included in our 2019 guide.

As we look ahead to 2019, we know the playbook that has worked best for LHC Group over the years: industry-leading quality scores, strong organic growth and capturing incremental margin improvement from acquired locations. You will see much more of that this year. You can also expect to see us maintain a disciplined approach to capital allocation, accelerate our plans for upside opportunities from building out our national platform, maintain momentum from innovative model arrangements with managed care initiatives and maximize the value of our health care innovation's business.

That concludes my prepared remarks, and I'm happy to further answer any questions during the Q&A section. I'm now pleased to turn the call over to Don.

Donald D. Stelly - *LHC Group, Inc. - President & COO*

Thank you, Josh, and good morning, everyone. Yes, what a great year for LHC Group in 2018, and we have another year of growth ahead of us in 2019. As my colleagues, I too want to thank our 32,000 team members who make that happen each and every day.

We are executing well on all fronts with the Almost Family integration. Organic growth and our quality scores again show sequential improvement. How best to judge our progress in these areas? We'll let the results speak for themselves.

For the Almost Family integration, we have compiled key performance indicators we are tracking. We've listed these KPIs in our new supplemental information on Page 18. From these stats, you will see that the admissions are up year-over-year, contribution is increasing and the number of Almost Family agencies rated 4 stars or better were up to 74% at December 31, 2018, up from 72% at September 30 and 68% at (inaudible) 30. The most important point that I can note here on the integration is that we are talking about how all of this work puts us in more of a growth mode and a more compelling joint venture partner. These are the strategic conversations and get to the real rationale for why we acquired Almost Family in the first place. The cost synergies have certainly been beneficial and will continue to do so -- be so in 2019. The more consequential conversations and discussions are what happens from here and that's what has us excited.

The transformation phase that Keith mentioned earlier gets to the heart of putting us in growth mode. This phase includes specific strategies to pursue new growth opportunities through market expansion and extension of our colocated and tri-located service offerings. In our minds, this is fairly low hanging fruit that we can go after as virtually untapped at this point. We will begin to do so as the year progresses.

Another area where we can leverage our more national platform is through additional acquisitions to fill specific needs and enclose new joint ventures with both small and large hospital and health systems.

Looking at our organic growth, we had strong results again in the fourth quarter. Home health admissions were up 7.8%, and hospice admissions were up 9.2%, which were both above our targets of 5% to 7%. For our 2019, we are targeting similar growth as we begin to see more of an impact from bringing our acquired locations up to our standards. This is the real engine of our growth and is likely the most attractive to our partners and investors alike. We will bring it all together with our quality stores, and we continue to shine there as well. We've outlined all of these scores on Pages 20 through 21 of the supplemental, but I would highlight in particular that our same-store LHC quality scores were up to 4.75 from 4.74 in October, and Almost Family improved as well up to 3.63.

Thank you again to all of my LHC Group family and our colleagues and also for you listening in to the call today. Christie, we are now ready to open the floor up for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Brian Tanquilut of Jefferies.

Brian Gil Tanquilut - *Jefferies LLC, Research Division - Equity Analyst*

So I guess my first question is on the joint venture. So you guys announced Geisinger earlier this week. So how should we be thinking about the remaining opportunity for JVs in the pipeline and how you think you can continue to ramp organic growth within the JV assets? And also just if you can give us more color in the Geisinger agreement and the rollout plan and the growth strategy for that market?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Sure. So we'll tag team that a little. I'll ask Josh to help me with that. Josh has been very involved on the Geisinger joint venture. But so on the JV strategy, we're -- if it's possible, we're more bullish on the JV strategy today than we've been in the past even, and we've been very bullish on it in the past. But I think more bullish because we continuously learn and improve our processes, and we learn a lot more from larger systems. They're harder. They have much harder hurdles to overcome in terms of different payer mix and value-based models that they challenge us to participate and perform in. And so when we have the opportunity to bring those skill sets that we learned in places like Ochsner over a number of years and then bring that to a joint venture like with an Ochsner -- like a Geisinger, I'm sorry. And there was a process. They were looking at other people in the process. But for me, it was rewarding to see us participate in that process and be able to respond to all of the things that were important to them and to win that process and understand why we won the process, knowing that it's based on our capabilities and performance, not on salesmanship or any politics that are involved. And I just want to say that as a compliment to the whole team, and it's something I feel really good about. The thing that I'm excited about looking forward is the number of inbound calls that we are getting today. For those of you who have been with us for many years, you know that when we did the first hospital joint venture in 1998, we were doing something that wasn't well known and that weren't very many around at all. And now we've created a component of our business model that's very much mainstream, and the majority of our pipeline is made up of calls that are coming inbound to us. And a decade ago, the opposite would have been true. The majority of our pipeline was made up of corporate development activities where we were going out knocking on people's doors. So that says to me that we have real momentum behind it. It's something that we do exceptionally well. We've developed a model that can be replicated. And in terms of organic growth, we really like it because we could see where the organic growth is going to come from in the future simply by looking at the number of lives that these health systems are caring for. And as we plug ourselves into that system and create value and earn that business through leading quality scores and patient satisfaction, the models become very predictable. Josh, you want to add anything?

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

No, Keith, that's great. Brian, great question because Geisinger is such an exciting opportunity for us here at LHC Group. I mean, as everyone is well aware, they have such a strong reputation and brand in the Pennsylvania and New Jersey markets. So couldn't be more excited that they've chosen us to be their partner. I have been working very closely with their executive team for the better part of a few months, and the momentum we already have in advance of an April 1 closing in Pennsylvania and ahead of June in New Jersey on the integration planning, the transition planning, identifying opportunities for improvement is well underway and probably a little bit ahead of schedule compared to some other conversations and acquisitions we've done previously. The other thing that I would note and highlight about Geisinger that makes it really unique and quite exciting as a little bit of a more innovative partner that they've already exhibited in the conversation we had with them is not only is the $35 million run rate revenue, and it's in these great markets with a great partner, but they're also affiliated with their own health plan, with Geisinger health plans. And the conversations around the managed Medicare as well as the managed Medicaid products coming in and bringing our clinical programs and bringing our quality scores and readmission capabilities is really going to take that JV to somewhere over the next few years where you're going to be hearing us talk more about the results.

Brian Gil Tanquilut - *Jefferies LLC, Research Division - Equity Analyst*

Appreciate those comments. Just a follow-up on that, on the slide deck. By the way, good job with the slide deck. One of the things that you highlighted are the different contracts with Medicare Advantage plans or private payers that you're working on with risk. So if you don't mind just walking us through how we should be thinking about the downside and the upside potential in those contracts that are underway.

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

Yes, great question, Brian. As we talked about on the last call, we're really monitoring our managed care improvements across 3 areas, improvement in rates and we are continuing to see incremental improvement there both on the LHC side as well as the Almost Family side, margin improvement in the underlying business. But to your point, Brian, it starts getting more interesting when you start coming up with new arrangements. And we've got probably 4 now that are finalized that have true upside potential within them, a little bit of downside but mostly upside, to be quite candid. And those arrangements have a little bit different components to them but at a 30,000-foot level, I would say they all have a base rate and then quality metrics that, if we achieve, we have the ability to generate savings and therefore earn some upside to that base rate. And it would be the quality metrics you would expect: reduced rehospitalization rates, emergency department utilization, things of that nature. But I think now that we have some and they're operating for a few months, as we head into '19, we've got some ammunition to go to other payers with some as evidenced [buys] to engage in more of these conversations and get more and more under the belt.

Donald D. Stelly - *LHC Group, Inc. - President & COO*

Brian, this is Don. Josh brings up an interesting point in -- you asked how should we think about the up and down side? I will empathically say that on the downside, it's around quality. And for years, we've said that once we find a payer that really is aligned with us, will deploy what we have to to achieve outcomes. So when and if you hear us continue to announce of these, I really wouldn't even focus on the downside because we're that confident of the programs that are going to underscore the value and get the top side payment for us, much like we've done in our ACO with Imperium.

Operator

Our next question is from Kevin Ellich with Craig-Hallum.

Kevin Kim Ellich - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

I guess, Keith, wanted to start off with Almost Family. Clearly, the integration is going well, ahead of schedule. We're coming up on you guys annualizing the deal in April. Just wondering if you can kind of talk about, compare and contrast how it's gone relative to your initial expectations when you announced the deal? And also, what surprised you the most about Almost Family, both positively and areas that could use some work?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

So I guess from a surprise standpoint, I feel like you want me to say something to you, but there were no negative surprises. But there were no negative surprises because of the incredible amount of diligence we did on the front end and the work streams that we developed with BRG in the diligence process way before we went live. So we didn't leave much to risk. So the biggest surprise, I think, for me then was the way that the cultures of 2 organizations that have been around for a really long time came together and really began to function as one team. I probably anticipate -- would have anticipated worse case and thought that there would be some rivalry and internal political battles we would have to fight, and we didn't face any of that at all. From day 1, for example, the division president from the Almost Family side and the division presidents from the LHC side, who obviously were rivals and competitors at one time, came together with a desire to learn from each other and to together identify the best practices and have everyone move to those. A lot of that had to do with leadership and messaging. My hats off to Don on that. Don did an incredible job of bringing the 2 together and creating one. Rather than walking in and saying, "Almost Family, welcome to LHC. We've got all the answers, now let us train you on what we do." That wasn't our approach. And you know, I think that's something about us culturally. We take that same approach when we go to a small hospital joint venture even though we may know some things that can help them, how we message that is real important. If you walk in on day 1 and you have a sense of arrogance about you, you're not going to be very successful. So I wasn't expecting this question so you're getting in on-the-fly, but those are my thoughts. Don?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

I echo everything Keith said, and there were no surprises candidly. And I think we were very open about that when we announced this deal and we were all sitting in Louisville. I will say a little closer to home, I'm very pleased that we have not one high-level leadership position open. We've remodeled, we restructured and we are smack dab in the middle of the homecare homebase optimization as well as on the home and community-based side that ContinuLink, which is going to be our platform moving from the legacy PCMS. Those are 2 instrumental components to finalizing this integration and poising the growth that both -- that all 3 of us actually in our prepared comments talked about. So in summary, I echo what Keith said. There were no surprises. The upside is already being recognized, and the back half of '19 sets up extremely well. And for those who follow us, you know we're conservative. And for us to be so out there and verbose on this should give you a lot of confidence in what we're feeling about this.

Kevin Kim Ellich - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

That's great, guys. I appreciate the candid remarks. And then going back to the managed care front, clearly, you've seen some success managing -- negotiating agreements with payers. In the slide deck again, we see the 7% increase for 2019 for your legacy business. Can you talk about the managed care environment? And I guess, are you done negotiating with the payers? Or should we see potentially some more [great] increase this year?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Kevin, you can ask me that question every quarter from now for years to come, and the answer will be no. We are not done negotiating. This is definitely a journey, but it's a journey that has more momentum and more optimism than this journey has had in the last few laps around the track. And it's the overall value proposition and the fact that the managed care payers now, whether it's evidenced by the improvements we're having in rates, these innovative models or as evidenced by what's going on in the greater kind of health care ecosystem, you can tell that the managed care payers now fully believe in the downstream benefit and the value of providing more care in the home. So when you finally have that breakthrough with them and they are, as you know, trying to bend their cost curve on a PMPM basis and they see us as a key component to doing that, the conversations are just a lot more strategic than they've been in the past. So the battle is not won. The negotiations are far from over but very confident and very encouraged about where we sit today and where we're headed. You overlay on top of that our position and where we stand out from a quality and readmission rate perspective, and that really positions us well as we're having those conversations.

Kevin Kim Ellich - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

Nope, that's helpful. And 2 last ones for me. First, you guys closed 22 centers or locations this quarter. Wondering if there's plans to see some more consolidation or closures that we should be thinking about. And then Josh, on the cash flow statement, it looks like there is some moving parts in working capital. I think AP and accrued expenses was a decent size use of capital -- or cash. I'm wondering if there's anything driving that and if that's going to reverse next quarter?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

This is Don. I'll take the first part. We would never want you surprised when we continue to close locations and here's why. Certainly, as we scaled, we find ourselves falling all over each other in states like Tennessee, Kentucky. Part of our monthly operations review process is to always look at sub-EBITDA agencies and look at the market in general and see by closing one, could we be more accretive in the market? Case in point, we're actually going to MORs right after this call. We will always look at that so that's just part of our discipline and rigor. I would say though when we do close than, we do analyze the goodwill. We take all of that into account to make sure it's still the best decision short and long term. So continue to do that and always will. So Josh will take the second part.

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

Yes. So on both on AP prepaid expenses, CapEx, in all those areas, you do see an uptick. A good portion of that is attributable to just the size of the company and the Almost Family business. There are some pieces to that, that won't be continuous and recurring. For example, some software costs, some IP contracts on bringing new licenses in for the Almost Family side of the business. And then you do have a piece of what's in the AP, for example, probably $4 million or $5 million of accruals related to our home office expansion project that is underway. You're going to see that coming throughout 2019 and into 2020 before we wrap that up. So that will impact our free cash flows to some extent. We still resulted with an adjusted free cash flow of $110 million for 2018. You would likely see us in the $140 million to $150 million range for 2019, but you'll have a little bit of pull on that free cash flow for the home office expansion. But that, as with every capital allocation decision we make, there's a very prudent, fiscally responsible, conservative financial reason we do those things. And just to give you a nugget on that, we are in a 67,000 square-foot building here at our main home office. We have 2 other locations throughout Lafayette, that's about another 40,000 square feet. We are consolidating it all into one project, eliminating a lot of lease and other costs. And at the end of the project, it will definitely be accretive to our bottom line as we go into 2020.

Operator

Our next question is from Joanna Gajuk with Bank of America.

Joanna Sylvia Gajuk - *BofA Merrill Lynch, Research Division - VP*

On the guidance, a couple of questions here. I appreciate the comment that the guidance assumes $25 million of synergies. So these are only the cost synergies, correct?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

That's correct, Joanna.

Joanna Sylvia Gajuk - *BofA Merrill Lynch, Research Division - VP*

So then, are you assuming any margin improvement on top of it that you mentioned on the prior calls in terms of the potential of moving margins on the AFAM assets higher? And also, are there any assumptions around revenue acceleration or any type of color what the guidance assumes around AFAM assets?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Sure. Sure. Great question. As you pointed out, the guidance is still anchored to the $25 million of realized cost run rate synergies. We are confident that we will exceed that by the back half of the year so there's a little bit of potential upside there. On the margin improvement, I would tell you, Joanna, from Q2 to Q3, we saw margin improvement in the AFAM business again from Q3 to Q4. We've already seen some, so a lot of that is already in the run rate. We have budgeted a little bit more incremental margin improvement on some of the AFAM assets that is reflected in our guidance. So you do have some of that lift as well. But some of the upside, if you will, for this year and beyond is really in the revenue synergies. Revenue synergies, either in growth as we come off the heels of the homecare homebase conversion and deploying some of our tools that we utilize for market intelligence and sales growth, as well as some of the colocated market strategies that we're deploying, none of that is in this guide, but that's for 2 reasons. One, we're conservative, and two, we may not see some of that until the late part of '19 and then really into 2020. But the growth we're projecting for AFAM is at 3.8% that we've realized this year. We are confident that will be able to continue to maintain positive growth, which is a welcome improvement to the AFAM book of business prior to the merger.

Joanna Sylvia Gajuk - *BofA Merrill Lynch, Research Division - VP*

Right. And then also on the guidance, one more piece in terms of the deals. How much of the deals that you announced recently were included? It sounds like maybe Geisinger is not included, but I guess could you just clarify that to us, too?

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

That's correct. So -- and maybe I'll go ahead and address just the revenue guide at this point as well in Q&A. So our guidance, if you look at Slide 19 in the supplemental deck, it lists a lot of JVs that have occurred since Almost Family. All of them, including Unity, the $4 million from Unity on an annual basis is included in our guidance. Geisinger, as we would never until it has closed, is not included in our guidance. So the -- from April to the end of the year on half of Geisinger and then June until the end of the year on the other half of Geisinger, none of that is in our revenue guide. Within our revenue guidance though, just to clarify a few points, the $30 million of annual revenue attributable to the 22 locations that we closed is obviously not in the guide and would be an adjustment, if you will, to the consensus on revenue. And then Eric and I had several conversations, and there has continued to be a little bit of confusion among a few folks around revenue before and after implicit price concession. So we are hopeful that we've kind of for once and for all, nailed down our revenue, made it real clear and guided appropriately for 2019 with all those variables in place.

Joanna Sylvia Gajuk - *BofA Merrill Lynch, Research Division - VP*

Great. That's helpful. And the last piece on the guidance. Are you assuming any additional spending as you prepare for PDGM? I guess you're prepared to talk about some changes there, so I just want to also hear how do you prepare. I appreciate the comments about the bill introduced in Congress and what kind of release it might get, but I'm assuming at -- I assume that you are assuming that the [reg] stays the way it is currently so how do you prepare? Are there any incremental costs that you could incur in 2019 as you prepare for 2020?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Great question, Joanna. And the short answer is that any costs are baked into the guidance that we've issued, and don't foresee a lot of costs, to be frank, but the ones that we do have are baked into what we gave you.

Joanna Sylvia Gajuk - *BofA Merrill Lynch, Research Division - VP*

All right. Are you doing anything specifically that you can frame for us in terms of are you preparing to hire a different set of caretakers? Are you doing anything around your staffing models or any systems that you might require? Or I guess, there's also some discussions out there in terms of the PDGM introduced new types of patients or maybe services to home health like behavior health? So anything there that you can flag to us as you prepare?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

This is Don. I think I'll be able to give you more detailed color that you're probably looking for as we go into the call. What I would say is, Keith alluded to the work streams that we developed in accordance with DRG to do the integration with Almost Family. We're actually excerpt in a playbook similar to that for PDGM, and we're developing work streams that looks exactly at what you're talking about. The types of patients and the required interventions and the discipline mix that we're trying to look at do that. That's at a very high-level and what I would call at work stream level right now, and our plan has us really having that ratio somewhere around June and July. So if you could give us the latitude to color in along the way, I think it will appease you.

Operator

Our next question is from Matt Larew, William Blair.

Matthew Richard Larew - *William Blair & Company L.L.C., Research Division - Analyst*

I wanted to ask about HCI. You mentioned one of your focus in '19 is to maximize (inaudible) of HCI. So what steps are you going to take in '19? And how did that manifest in terms of the potential acceleration in revenue or new opportunities you might see there?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

So this is Don. Let me start off with this is that the HCI service lines that make up the segment, when we did the merger, there was kind of a thought that some of them were loss leaders, and I know speaking of Joanna, she put that out in her note. We've taken a different view that each one of these has such a huge opportunity for the portfolio in general, but they have to live within their own budget and accrete. And I'm very pleased to say that, that progress has been made, whether it's our advanced care house calls, which was formerly MD2U. It had loss runs that are now corrected. Fabulous opportunity with Imperium. It's doing the same thing now on a PMPM basis so that the Medicare shared savings is not something that pays for the loss runs but is on top of it. And finally I couldn't speak highly enough about LTS in that segment. So from an operations perspective, Keith, Josh and myself as well as Bruce and others, said listen, "let's first get the fundamentals in a very congruent and like fashion with everything else in LHC Group and then let's take it out to market and do different things with it" and I'll let Keith expand on some of that -- or Josh.

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

I'll jump in specifically on Imperium. I know Don has really been doing a great job. Candidly, I want to give him a lot of kudos for the improvements already in advanced house calls and the LTS business. But the ACO business in Imperium and you've all heard me talk several times about our excitement for that, it was almost the diamond in the rough in the merger. The learnings that we're having there are going to pay dividends and bear fruit in all of the managed care conversations I alluded to earlier. It's the same -- it's the same approach, just with a different payer source. So what we are able to learn there is going to be very helpful in those negotiations and then in implementing and executing on those contracts. You're going to see incremental ACO volume growth in Imperium as well, both in new commercial contracts on the PMPM side as well as getting new ACOs into the product. We've grown from 16 ACOs in 2017 to 30 ACOs currently, and we've got 460,000 attributed Medicare lives, up from 140,000. So the growth has already proven evident, and I think the leadership team there, really with Bruce driving that now, is taking that to another level, and you're going to see more growth. And to Don's point, not just rely on the MSSP to make it profitable but to let it stand on its own as we get into the second half of this year and then the MSSP is just an additional incremental jolt in the third quarter.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Bruce, you have anything to add?

Bruce D. Greenstein - *LHC Group, Inc. - Executive VP and Chief Strategy & Innovation Officer*

I'll just add to what Josh mentioned. It's a bit of a training ground for our company to be looking at total cost of care across the total post-acute spectrum. So as we work with our ACOs, the ACO segment become a mine for data for as we look at Medicare expenditures across the entire continuum. We've recognized what the cost of this -- what the costs of the total post-acute care expenses look like for all of our ACO customers. And then from the ACO perspective, are coming up with solutions to be able to help manage costs for our ACO customers but the positive externality is, as a company, LHC Group gets to understand the spending patterns and know how to help out to those that are interested in managing the total cost of care for our managed care plans as well as the physicians that we work with within the ACO, and we're able to bring solutions from the home health side to our customers. So it's been positive for both sides. At the same time, we recognized efficiencies within the company of Imperium itself and have a much more positive financial outlook for the rest of the year. And as Josh mentioned, growing the business both on the non-Medicare side so in the form of commercial contracts with large payers as well as growing the book of Medicare and as the window opens for ACO enrollment later this year, we expect to see growth there as well.

Matthew Richard Larew - *William Blair & Company L.L.C., Research Division - Analyst*

This question may stick with you as well, which is on the personal care side here, with the Medicare Advantage rule change last year in April, maybe there wasn't quite enough time ahead of July for these plans to incorporate more broadly some of the supplemental benefit, but now that there's been a year under the belt, just wondering what type of conversations you might be having with payers in terms of using the personal care business to help them out there.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Yes. We're having 2 types of conversations. We had some that came in right at the wire for the 2019 filing date, and we are agreeing to be either a provider where the rates make sense to us, and we also are agreeing to work with our large -- most of these MA plans we work with as a provider on the home health side to start with. As they start to venture in the personal care services, it's interesting because the large plans mainly don't have a lot of experience in deploying these services. We have a broad range of experiences from our core group and then from the Almost Family markets as well. So over time, we're helping the managed care plans understand how best to use personal care services to use it across their post-acute services to manage total cost of care as well as make it a meaningful and affordable benefit to offer for the long run. So we continue to be in these conversations. We're working out our provider arrangements today. We expect there'll be a lot more for the 2020 service year, and those conversations are robust right now.

Operator

Our next question is from Patrick Feeley with Barclays.

Patrick Thomas Feeley - *Barclays Bank PLC, Research Division - Research Analyst*

One of your competitors was talking about seeing a little bit of star rating decline with the April release due to new measures that CMS is introducing in the program. Just curious if you expect to see any decline there in April. And also, just any update on how long it may take to get the Almost Family and recent acquisition star ratings up to where the LHC same-store ratings are trending.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

I would say that our internal system from SHP, which is a more concurrent monitor does not show that decline so I would not expect that in the aggregate. Certainly, some agencies slip up and slip down but so in the aggregate, I would not. As I told our board last week, putting our performance improvement structure inside of Almost Family has what incremental improvement been demonstrated from right now. But really, we don't anticipate substantive movement up to the LHC Group until each of the regions is finished 6 months after it's finished moving to the homecare homebase one instance. And the reason that's so important isn't about homecare homebase but the processes that dovetail in accordance with that from admit all the way through our end-of-episode audit process. So in totality, probably somewhere around April of next year of 2020, I would expect that all of those have very similar characteristics in star as well as ACH rate improvement in that portfolio.

Patrick Thomas Feeley - *Barclays Bank PLC, Research Division - Research Analyst*

That's helpful. And just a clarification. On the location closures during the fourth quarter, you disclosed those had about $29 million of run rate revenue associated with them. Just how much of an impact does that have in revenue in the fourth quarter? Were those out the majority of the quarter?

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

No, that was about $7 million, $7.5 million of revenue impact on the fourth quarter if you're trying the bridge to where we ended.

Patrick Thomas Feeley - *Barclays Bank PLC, Research Division - Research Analyst*

So they're pretty much out from the beginning.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Yes.

Operator

Our next question is from Frank Morgan with RBC Capital Markets.

Frank George Morgan - *RBC Capital Markets, LLC, Research Division - MD of Healthcare Services Equity Research*

You talked about the backlog of deal opportunities you see in your liquidity to be able to execute on those, but I'm curious what would you say when you look at that backlog? How is that skewed in terms of home health care versus hospice and personal care? And what should we realistically expect to see the most action for external growth across the balance of the year?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

I think the majority will be in home health just where it's a lot of the interest is coming from, and that's typically our lead in new markets. Of course, as is the case with Geisinger, when we go to Geisinger, we pick up both home health and hospice, where we're lucky if we get that. If we don't pick up hospice, then hospice moves to a buildout strategy for us. And buildout, in our mind, is not a startup but buying a small or regional hospice and bolting it on to -- and potentially rebranding if appropriate. And then personal care is a little harder work because, as you know, each state is different, and you have different reimbursement and different market opportunity, different margin in every state. And so we -- there are some states that we're more bullish on building out a personal care platform than others. There are a lot of things that we take in consideration in the scoring and prioritization of states.

Frank George Morgan - *RBC Capital Markets, LLC, Research Division - MD of Healthcare Services Equity Research*

The second question, I apologize for being all over the place here. But you talked about the conservatism in the guidance and the fact that Geisinger is not in your guidance. But just for the record, when that closes, will that actually be accretive to 2019 once it closes?

Joshua L. Proffitt - *LHC Group, Inc. - CFO*

No, Frank, it's Josh. That's a great question. It's not in the guidance at all. And what I was referring to in Joanna's question, I was talking about revenue, I would not bake anything for Geisinger to be upside to 2019. 2019 is very much going to be kind of the transition stabilization and get that one ready to be accretive and additive in 2020. It's not going to dilute, but it should not be accretive either.

Frank George Morgan - *RBC Capital Markets, LLC, Research Division - MD of Healthcare Services Equity Research*

Got you. One last one and I'll hop. You talked about some of the risk arrangement. I think Kevin asked about those, and you talked about the base rates and the bonuses there. How are those base rates structured? Are those per diems? Or are those episodic rates? Maybe any color there then I'll hop off.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Frank, they're some of both. There are some that are episodic with an upside, and then there some that are per visit with upside. So we have some of each.

Operator

Our next question is from Whit Mayo with UBS.

Unidentified Analyst

This is Nathan on for Whit. You mentioned the colocation strategy a couple of times. I think the slide deck said you expect to accelerate that. Is there any more detail you can give us around both in terms of pace, what it could mean from cost savings or revenue growth perspective? And then is that more about acquiring or building hospice assets where you already have home health? Or are you looking at existing overlapped markets and consolidating some of your existing agencies into a single location?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

That's a really good question, and it's actually the latter first. The first part of this approach is where we have multiple assets we want to co-locate them and kind of a create a one domain, if you would. And how I would look at that versus the pace of acceleration, that is part of our organic build up that we lead to in the 5% to 7% for home health and the 6% to 8% for hospice. So it's kind of baked in there versus saying how many locations or how many markets, I can do that. We've identified literally 72 different markets. But the way we go about it, really, because we budget our organic growth by market by location, that is really underscoring those 2 values that I've talked about. As for the way we go out and Keith alluded to it earlier and the buildout strategy in the Geisinger example he gave, that is something we got to go acquire, and that is kind of outside of our normal purview of the operations that we put in the deck.

Unidentified Analyst

And so it sounds like this is a little bit more around a top line opportunity rather than just the cost savings of us having a single building?

Donald D. Stelly - *LHC Group, Inc. - President & COO*

It's absolutely that because on the cost savings, you may lose a little G&A from a building and the rent. But your infrastructure, which is the leadership mostly, still has to be in the same 4 85s and other regulatory paperwork and that doesn't go away. This is all about underscoring the long-term organic growth proposition.

Unidentified Analyst

And just a clarification on PDGM and the behavioral adjustments. If the industry did not make the behavioral adjustments to the extent CMS is modeling, they would essentially just have to give you an extra increase in 2021 to make up for that to keep it budget-neutral, correct?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Yes. I mean, in theory, but the intention is that it's budget neutral. And if it results in year 1 in a cut, then that would then come back the next year and recalibrate it and keep that from happening again. So that definitely is the intent, Nathan.

Operator

Our next question is from Dana Hambly with Stephens.

Dana Rolfson Hambly - *Stephens Inc., Research Division - Research Analyst*

You mentioned a couple of times the conservative nature. And historically, LHCG was a pretty consistent beat and raise, and 2018 was in line and a great result but probably a bit choppier than most of us who have been following you for a while would have expected. So just curious, do you think -- was AFAM a challenge for you in visibility last year? Or was it more around ASC 606 and divesting some things? And do you feel a lot better about your visibility on AFAM this year? Or do you think this is just not a fair observation?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Dana, it's a very fair observation. And you've been with us for a long time, and you're right. And I would say 2018, from a financials perspective, was I'll use your term, a little choppy. But the visibility and the live sight we now have as we head into '19 could not be more clear. So again, very pleased and proud of the team to deliver what we did deliver in '18. As we said, when we reissued guidance when we consummated the AFAM merger, we put it out there with a range that could potentially get you up in the 14% accretive range and we delivered that. Now it may have been a little choppy along the way, and there may have been AFAM lack of visibility, but I'll tell you that where we sit here going into the future, I think you've got core LHC Group and our principles and our conservative nature is where we sit here on February 28.

Operator

Our next question is from Matthew Gillmor with Robert Ballard.

Matthew Dale Gillmor - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

First one on guidance. I was curious with the agency closures. Is there any opportunity for you to recapture some of that revenue with other agencies? And is that perhaps a source of conservatism in the guidance? Or is the nature of those closures mean that you're just not going to be able to recapture some of the revenue?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

No, Matt, that's a great question. And I would say probably in half of the locations, you have that opportunity where it may have been overlap situations with the legacy AFAM and a legacy LHC location, for example. So you have one underperformer, you close it. You eliminate all the G&A and the loss runs. And then over time, you go back and rebuild the market share. So there will be some ability to build some of that back. That's a good observation.

Matthew Dale Gillmor - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. And second one just on the PDM strategy question. Obviously, the joint venture strategy you all have could provide some real advantages because there's more reimbursement dollars associated with referrals from the inpatient setting. Can you just sort of update us on the percent of referrals you get from your JV hospitals or that collaboration rate and sort of what would be the opportunity going forward?

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Yes. That's a really good question. So there are -- so think of the number of referrals and I don't have the exact stats in front of me, but probably close to 50% of the admissions we take into the company now come from -- come out of hospitals and about 50% from the community. Let me say a little bit about that. So in every joint venture that we are in, we don't rely only on the patients that are being discharged from the hospital. Part of what the hospital partners want from us and don't have when we go in, we go in and we inherit a home health -- a hospital-based home health operation where essentially 100% -- nearly 100% of the admissions of home health agency are company from discharges from the hospital.

They're not reaching out to the community and providing care for patients who may need home health on a pre-acute basis, to avoid hospitalization in the first place. For those partners that are focused on value-based models in population health, that becomes really important. So that's something we bring to the table. I first want to make sure that you and everyone understands that. On the -- now back to your question though. It is true that there's more favorable reimbursement for patients being discharged from a hospital. We should incentivize patients to move out of the higher-cost setting to a lower-cost setting. And we're investing more resources in transitional care, and that aids our hospital partners as -- to identify those patients that are appropriate for home care and that can move downstream from more costly settings to home health, not just being discharged from the hospital earlier but avoiding other post-acute verticals on their journey to home health and moving to home health more frequently, bypassing mainly SNIFF or SNIFF and at times, IRF and going straight to home health. That's the real role that we're playing long term. That's such a great question.

Operator

Thank you, and that does conclude our Q&A session for today. I'd like to turn the call back to Mr. Keith Myers for any further remarks.

Keith G. Myers - *LHC Group, Inc. - Co-Founder, Chairman & CEO*

Okay. Thank you, operator. Thanks, everyone, for joining us this morning and for your excellent questions. As always, if you would like to speak with us at any time between earnings calls, Eric Elliott is available to take your call. And if you need contact directly with members of the management team, Eric can arrange that. We want to be here for you to answer questions. So again, thank you for joining in, and thank you for support of our LHC Group family. Have a good day.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program and you may all disconnect. Everyone have a great day.
