AdaptHealth
Second Quarter 2021 Financial Results Conference Call
August 5, 2021

Presenters
Christopher Joyce, General Counsel
Steve Griggs, CEO
Josh Parnes, President
Jason Clemens, CFO

Q&A Participants
Brian Tanquilut – Jefferies
Pito Chickering – Deutsche Bank
Matthew Blackman – Stifel Financial Corp.
Courtney Fondufe – Bank of America Merrill Lynch
Eric Coldwell – Baird
Richard Close – Canaccord Genuity

Operator
Greetings. Welcome to the conference AdaptHealth second quarter 2021 financial results conference call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press star zero on your telephone keypad. Please note this conference is being recorded.

I will now turn the conference over to your host, Christopher Joyce, general counsel. You may begin.

Christopher Joyce
I'd like to welcome everyone to AdaptHealth Corp.'s earnings conference call for the quarter ended June 30, 2021. Everyone should've received a copy of our earnings release earlier this morning. If not, I'd like to highlight that the earnings release, as well as a supplemental slide presentation regarding Q2 2021 results, is posted on our investor relations page.

In a moment, we'll have some prepared comments from Steve Griggs, CEO; Josh Parnes, president; and Jason Clemens, chief financial officer. We will then open the call for questions.

Before we start, I'd like to remind everyone that statements included in this conference call and in our earnings release 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 2020 and beyond.

Actual results could differ materially from those projected in forward-looking statements because of a number of risks, factors, and uncertainties, which are discussed in our annual and quarterly SEC filings. AdaptHealth Corp. shall have no obligation to update the information provided on this call to reflect subsequent events. Additionally, on this morning's call, we will reference certain financial measures, such as EBITDA and adjusted EBITDA and adjusted EBIDTA less patient equipment capex, which are non-GAAP financial measures.

This morning's call is being recorded and a replay of the call will be available later today.

I'm now pleased to introduce our CEO, Steve Griggs.

Steve Griggs
Thank you, Chris. And thanks to everyone for joining our call. This week marks the first six months for the combination of AdaptHealth and AeroCare. Our original thesis has been confirmed. We are in a business with secular tailwinds since more and more healthcare is being delivered and monitored in the home. And we have proven that we can grow both through acquisitions and organically.

Accordingly, by combining our companies, we envisioned we would improve patient access, patience experience, and clinical outcomes. With this vision in mind, we continue to execute on our strategy of organic growth, improving operations, and closing accretive acquisitions. We do this by leveraging technology and workflow to improve our operations and have already achieved significant direct and indirect cost savings via purchasing volumes.

In addition, six months into the combination, we've seen great progress towards our synergy plan, including consolidating 88 locations and implementing our digital logistics and RCM platforms. Our synergies activities are substantially complete. We remain confident in our previously communicated synergy target of 50 million annually and 30 million in 2021.

On the sales front, we made strong progress reorganizing and focusing our combined 615-person salesforce. As part of this reorganization, we have taken the best training, tools, and practices and applied them across the entire business. We believe through the--through our sales efforts and the resupply engine, we will maintain an organic growth rate of eight to 10 percent over an ever-increasing base.

Most importantly, by combining our operational teams and leaders at all levels across the country, we believe that we will be more powerful than the sum of our parts and pursuing our mission to empower our patients to live their best lives out of the hospital and in the home.

The success of our combined team is evidenced in reaching our highest reported revenue and adjusted EBITDA margin for this quarter. So far in 2021, we have accelerated our acquisition pace. When we acquire a company, we not only evaluate the near-term and longer-term cash flow characteristics of the target, but equally, or more importantly, how it will fit into the ongoing organic growth profile of the company. An example of this is our Q2 acquisition of Spiro Healthcare in New England. Prior to the acquisition, neither AeroCare nor Adapt had significant operations in this geography. As a result, we expect to grow significantly in this region.

In addition, we completed three more acquisitions in the second quarter, one being the acquisition of Healthy Living Medical Supply based in Michigan. We are very excited as we continue to expand our diabetes presence with this acquisition.

Already in the third quarter, we have closed six more acquisitions, each one meeting our criteria for earnings and strengthening our strategic presence in existing regions. With these additions, we expanded our operations in Kentucky, Ohio, West Virginia, New Jersey, New York, South Carolina, and Florida.

The second quarter started with broad COVID-19 vaccine access across the country and the reopening of our economy. The reopening was evident in the referral patterns of our hospital and health system partners as elective procedures came back and pent-up sleep study demand was met.

However, the emergence of the delta variant of COVID-19 has raised concern in our economy's overall recovery. We demonstrated our ability to respond since the beginning of COVID-19 pandemic, and we are confident in our ability to continue to respond as necessary.

In addition, we generated 9 million of revenue in the second quarter from B2B sales, supporting our hospital and health system partners and providing much-needed oxygen and ventilation equipment. Although we do not expect this revenue to be recurring, it continues to demonstrate the commitment of our workforce in serving the needs of our partners and patients.

In summary, we are very proud that the past six months has validated the future that we envision for our patients, referral sources, employees, and shareholders. Now, I'll turn it over to our president, Josh Parnes.

Josh Parnes
Thanks, Steve. My remarks will focus on the key aspects of our strategic road map, including operational technologies, chronic disease management, and how these capabilities help enhance our overall business. I'll also comment on our diabetes integration and growth progress. But first, I'd like to discuss the operational impacts of the Respironics recall announced by Philips on June 14, 2021 that is affecting the entire sleep health industry.

Philips Respironics has been a great partner of ours for years, and we're committed to working through these challenges together. For our business, there are two operational areas. The first is patients currently on billable census with products on recall and the second is the supply chain for the new devices that could potentially impact our ability to meet new start demand.

We have several levers available to mitigate the potential shortage, including inventory management, asset recovery, and alternative suppliers. There was no financial impact to Q2, but we believe the potential impact to the second half of '21 could be up to 30 million of net revenue. We expect much of the shortfall in setups would be delayed until 2022 and likely recaptured, and we'll have a better perspective on this by the time we report next quarter.

Turning to the key aspects of our strategic road map. We're very pleased with our continued adoption of our e-prescribe technology. For example, in our diabetes product line, approximately 40 percent of new orders are currently flowing through this technology and more importantly, our cycle times are down significantly. This reduction in cycle time drove improved patient and provider satisfaction.

We have advanced one of our key technology synergies between Adapt and AeroCare. Our proprietary real-time end-to-end logistics delivery platform enables mobile-friendly order tracking and communication with our patients. This technology is the backbone of our CRM system used by our sales reps and has been rolled out across the vast majority of the organization.

Continuing with our strategic road map, our long-term goal as a leading home care provider is to continue evolving our service model to more efficiently help patients manage chronic illness in the comfort of their own homes. Several programs are underway focused on our sleep, COPD, and diabetes patients, including technology-enabled coaching and chronic disease management to drive a better disease outcome over time.

For one example, we have enrolled several thousand patients in our COPD disease management program, which develops individualized plans of care and provides patient clinical data reporting to physicians. This technology has already proven significant reductions in hospital readmission statistics. Additionally, this program simplifies workflow and drives efficiencies for our several hundred clinicians who serve patients in their homes.

Improving patient experience and outcomes is a core principle at AdaptHealth. Accordingly, we will continue to invest in both talent and technology to further improve outcomes and reduce the overall cost of care. With these investments in technology and chronic disease management, we are accelerating growth in all of our product categories, most dramatically in diabetes, our fastest-growing product category.

Coupled with our e-prescribe platform and proprietary intake technology, we believe we are growing in line with the overall end market. We have combined our national diabetes sales force with our hard-earned expertise in HME resupply operations to accelerate organic growth in each of the six businesses we've purchased since last July. We continue to be extremely excited about the future opportunities within this product category.

With that, I'll turn it over to Jason to discuss our financial results.

Jason Clemens
Thanks, Josh. Good morning, and thanks for joining our call. For the second quarter ending June 2021, AdaptHealth reported net revenue of $617 million, an increase of 166 percent from the second quarter of 2020. As detailed and defined in our Q2 2021 earnings supplement, AdaptHealth's organic growth for the quarter was 10.1 percent, supporting our long-range organic growth estimate of eight to 10 percent.

This growth was again led by new starts in our diabetes product line and continued strengthening in our sleep business, following the lull of new starts impacted by the pandemic in mid-2020. As a frame of reference, pro forma net revenue for the quarter was $632 million, driven primarily by Spiro Health Services and Healthy Living. Beginning in Q1 2021, our pro forma net revenue disclosure in our Form 10-Q includes all acquisitions completed in the period as opposed to just material acquisitions, which were previously disclosed. We intend to maintain this increased level of disclosure going forward.

Turning to profitability. Our adjusted EBITDA was $148 million for the quarter, resulting in an adjusted EBITDA margin of 23.9 percent, up from 21.6 percent in the first quarter. We benefited from a full quarter of AeroCare that historically delivered higher margins than the stand-alone AdaptHealth business. Additionally, our synergy program continues to roll along and is absolutely on track, contributing to higher margins for the quarter.

On the regulatory and governmental front, there have been a series of positive announcements across our industry. First was the extension of the public health emergency announced on July 20th. The extension will provide continued reimbursement benefit for the next 90 days when the extension will be reevaluated. Our updated guidance includes the current PHE extension, but it does not include any future extensions.

Additionally, CMS announced relaxed standards for CGM qualification, removing the four per day test trip requirement. Some commercial carriers have already followed suit, mirroring the CMS policy.

Finally, and very importantly, CMS published a proposed rule calling for relaxed qualification standards for oxygen, including possible elimination of the chronic stable state requirement and possible elimination of the CMN, or certificate of medical necessity. The industry has supported this change for many years, and we're pleased with the proposed changes.

We think it's unlikely for these guideline changes to result in a material increase to revenue in 2021m but as we get more data behind us, we will certainly evaluate these announcements as part of our 2022 financial planning cycle that just kicked off.

Turning to the balance sheet. We prepaid half of the outstanding principal on our 12 percent interest promissory note. We expect to pay down the remaining principal between now and September 30th. We had $175 million outstanding on the revolver at the end of the quarter. We're pleased to take this next step forward in simplifying our capital structure and refinancing expensive debt.

We are also focused on driving increased conversion of adjusted EBITDA to cash flow from operations. Speaking of that metric, we generated 147.6 million of cash flow from operations for the first half of 2021. This included 15.9 million of cash outflow associated with CARES Act recoupment during the second quarter, representing about a third of the 2020 advanced payment that will be returned to CMS.

Overall, we are very pleased with the amount of cash our business is generating and remain in range of our previously discussed expectation of converting approximately two-thirds of adjusted EBITDA to cash flow from operations.

I'd like to turn to our updated guidance for 2021. As announced this morning, we are increasing our 2021 full-year guidance for net revenue, adjusted EBITDA, and adjusted EBITDA less patient equipment capex. We are guiding to net revenue of $2.38 billion to $2.48 billion, adjusted EBITDA of $555 million to $580 million, and adjusted EBITDA less patient equipment capex of $360 million to $375 million. This increase includes 90 to $100 million of in-year revenue for the additional acquisitions announced today.

As a reminder, our previous guidance included in-year revenue for Spiro Health Services. We also included in our estimate a potential Philips Respironics device shortage of up to $30 million of revenue. This situation is fluid, but we are confident we'll have enough clarity to assess any possible impact to 2022 by the time we report next quarter.

As a reminder, our guidance does not include any contribution from acquisitions that have not yet closed.

I have one more important topic to discuss. We continue our progress transforming our back-office operations, including the installation of new technology and capabilities. Our ERP met our Phase 1 go-live on June 1st, and all other transformation streams remain on track.

With that, I'll turn it back over to Steve.

Steve Griggs
Thank you, Jason.

Before we turn to questions, I'd like to thank our 9,068 employees across our 678 locations for their contributions to a successful second quarter. Also, we appreciated their continued commitment, passion, and excellence toward advancing our strategy of organic growth, improving operations, and accretive acquisitions. Thank you. And now, let's open up for questions.

Operator
Thank you. At this time, we'll be conducting a question-and-answer session. If you would like to ask a question, please press star one on your telephone keypad. A confirmation tone will indicate your line is in--you may press star two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys.

Our first question comes from Brian Tanquilut with Jefferies. Please proceed with your question.

Brian Tanquilut
Hey. Good morning, guys. Congrats on a very solid quarter. I guess I'll start off with a question, let's address the elephant in the room. I guess, for Jason, a lot of people have been asking us about your organic growth mask.

Any clarity or any other color you can share with us? And maybe some visibility into, you know, what Q1 and Q2 would have looked like, you know, using more traditional organic growth mask? Just address that point that a lot of investors have been focused on.

Jason Clemens
Sure, Brian. Good morning. Well, first, I'd start with the continued and increasing disclosure that we're bringing to our 10-Qs. You probably heard that in my prepared remarks.

As part of Q1, right, so this is prior to any of the kind of various reports that might be out in the market over the last several weeks, we made a change to how we disclose acquired revenue. We've now included every dollar of acquired revenue in the quarter. Historically, the company had included only material acquisitions. And so, not all dollars were included.

So, that is a change. We think it's just better visibility and transparency. You will expect to see that in our 10-Q that we will file following the call and also going forward.

So, the second thing we did in terms of added disclosure, you'll see on our Q2 supplement that we posted to the AdaptHealth website early this morning under our investor relations page, you'll see page seven, a continued bridge of organic growth. We start with reported net revenue growth, right? So that's the 617 that we reported this quarter against the prior year of 232.

The next step that we're demonstrating is pro forma net revenue. And so that, again, is included in our Q, right? It's the definition that you'd expect. It's just the standard ASC 805 definition of pro forma revenue, and that's showing 632 of Q2 against 572 on the prior year.

The next step--so, in our definition of organic growth for the company, we've made two adjustments. The first is B2B revenue. I mean, I think it's no surprise we continue to exclude that from our kind of analytics. It's not recurring revenue. We're very proud of it, as Steve said in the prepared remarks, but we don't include it or assume it's a go-forward contribution to the company.

The second thing we demonstrate is there's a difference between pro forma--the formal definition of pro forma revenue versus acquisitions that AeroCare made from January 2020 until we acquired AeroCare. So, as you all know, AeroCare was highly acquisitive, and so we've pulled those acquisitions out. We think it gives a somewhat distorted view of growth if that's counted in. And so that's the final adjustment we've made. So, again, that full bridge is included on page seven of our supplement.

In terms of--I think when you say traditional same store, you might be alluding--or I'm sorry, when you say traditional organic growth, you might be alluding to same store. I'm going to pass that to (INAUDIBLE)--yes--yeah, I'm going to pass it to Steve to reiterate why that's not a metric that we use to run our business.

Steve Griggs
Yeah. Thanks, Jason, and Brian, too, for the question. So, first, I just want to be clear and reiterate our belief that our business will grow eight to 10 percent. We expect existing businesses and including the acquisitions to grow eight to 10 percent.

So, our managers out in the field are incentivized to grow their revenue level, not what they had three or 12 months ago. So, if a regional leader has a $100 million revenue base and we acquire 20 million in revenue in the region, we're looking at incentivizing them to grow $120 million in revenue. And so, whatever that point is, we look out, you know, 12 months and say that should grow eight to 10 percent or whatever level we have in store for them.

So, when you talk about same-store growth, we just don't manage that way, and we don't account for it that way. I'll give you an example in the state of Texas. You know, Adapt had business in Texas in 2019 and in 2020, they acquired a very good business in Healthline. Almost immediately, the integration process started combining locations from legacy Adapt into Healthline and back and forth. And then, they're doing a few other smaller acquisitions, and all those got combined into the existing operations.

Then, in February, AeroCare was purchased. We had a very large presence in Texas, almost equal to the Adapt. And as we indicated, with AeroCare and Adapt combining offices, Texas was no exception. Multiple offices were merged together.

So, our Texas regional leader doesn't try to manage growth for a particular location or a particular time. She manages the entire region. And now the merged region is significant for her and her goal for her and her sales manager is to grow the combined region eight to 10 percent. And while at the same time, making it more efficient.

So, that process right there makes it extremely difficult, I would argue almost impossible, to calculate a same-store growth because there's no more same stores. They've all been merged in together. And so, that's why we look at what are we at today and we want to grow that business. Does that make sense?

Brian Tanquilut
Yeah. No, that's great. I really appreciate that. And thank you for all that color.

And I guess my next question, since I have you, Steve, you know, I think at the beginning of the year, when we were looking at your long-term growth targets, one of the things you guys mentioned was trying to buy 100 to 150 million worth of revenue a year. You're already at 300 million this year. So, clearly, you've demonstrated your ability to acquire your intent to maintain, you know, a robust pace of M&A.

So, should we be thinking that there's more in the pipeline? And how are you thinking about, you know, the integration of these deals and just, you know, the ability to bring them in and continue growing these assets that you're acquiring?

Steve Griggs
Yeah. I mean--so, right now, the pipeline is very large. Surprising to me somewhat that we have this many of really, really quality assets that AeroCare coveted to have a chance to--you know, prior to this and Adapt did, too. So, I think the acquisition activity is going to be, you know, pretty robust for us for the, you know--for the rest of the year and into 2021--2022.

So, how do we combine them? Well, the acquisition work and the part of that is already done for AeroCare. So, that team is available to work on other acquisitions. And then, when we start combining them and integrating them, well, that's mostly done by the local managers and the regional managers.

So, for instance, if they're going to--if they're working on that and they're working on this particular acquisition in the state of Texas, for example, and they get that done, well, you know, we might have an acquisition going on in Tennessee. That's a whole different team that's making sure that that gets, you know, combined and integrated in their operations.

So, as long as we're not piling them up on top of an operational team one after another, which we don't do, we should be able to handle that fairly efficiently.

Brian Tanquilut
Got you. And then, my last question for Josh. In your prepared remarks, you talked about how you feel like you can grow in the diabetes space, you know, together with the market. And I think DexCom's out there with sort of a five-year guidance of, like, you know, 20 percent volume growth.

So, is that--and I know your guidance is in the 10 to 12 percent range for, you know, kind of long-term growth here in diabetes business. So, is that just still being conservative with a view on diabetes? And is the 20 percent kind of the good near-term number to be thinking about?

Josh Parnes
Yeah. Thanks, Brian. So, I think, you know, our diabetes businesses, just as a reminder, is a smaller portion of our overall business. So, even if you were going to get a higher organic growth number there, it nets into kind of eight to 10 percent over the entire organization.

But, you know, diabetes for us has been--you know, we've been in it for about a year now, and it's been great. You know, out of the gate, we've been pushing e-prescribe and all the things that we've learned on the HME side of the business. I think about, you know, resupply, e-prescribing, some efficiencies on intake technology, and that's really allowing our prescribing partners and physicians to really get a much more efficient experience. And also, under the medical benefit as well to really drive efficiencies in that process and the documentation process.

So, that's then allowed us really to grow with the market, and DexCom and others are out there saying it's 20-plus percent. We believe that, you know, we can grow in line with that. Over time, our goal certainly is going to be to take market share. But, obviously, we're generally new in the business and we're learning as we go, but it's been a really great start so far.

Steve Griggs
Yeah. And I would add, Brian, that--to Josh's comments, you know, we've got six fantastic businesses that we're now running. We're an integrated platform. But the first one was acquired just July 1st of last year. So, you know, we're just getting into this business now for a little over a year.

As we had said on previous calls, as we get a little more data behind us, if it continues--our trends continue and we are indeed above that 10 to 12 percent, you can expect us to refresh that perspective as we start talking about 2022 guidance as we'll do in about 90 days from now.

Brian Tanquilut
Awesome. Congrats again. Thank you, guys.

Operator
Thank you. Our next question comes from Pito Chickering with Deutsche Bank. Please proceed with your question.

Pito Chickering
Hey. Good morning, guys. Thanks for taking my questions. Two quick ones here to start off with. Looking at the revenue guidance from December when you guys acquired AeroCare, you had 2.05, $2.2 billion of revenues, and then compare that to the new guidance of 2.38 versus 2.48.

You said in your press release that you have acquired $300 million of annualized revenues, which obviously didn't all close in the first quarter. Just, you know, how much revenue have you guys acquired since that announcement? Just trying to sort of bridge, you know, organic growth rate versus that acquired growth from, you know, the December guidance to today's guidance.

Jason Clemens
Hey, Pito. This is Jason. I'll be glad to take that. So, you know, we had three separate raises since the AeroCare announcement. In terms of revenue, if you recall, Q4 2020, we raised 130 to 150 million of revenue. That was for the five deals we acquired from December 30 through that earnings call.

The next raise was the last call. We talked about Spiro, and there's also--there are some dollars in there for the CMS oxygen fee schedule rate increases that went into effect April 1st. That was a $40 million raise. And then, today, in my prepared remarks, I talked about raising 90 to $100 million for acquisitions.

So, I think, you know, if you take that all together, you're looking at 260 to 290 ballpark for acquisition raise. That's in year. So, to the point of we've acquired over 300 million of annualized, that's where that's coming from.

The one item I will call out is the Philips impact, right, that's netted in there. But otherwise, you know, those are the acquisition numbers.

Pito Chickering
Okay. Which is a nice sort of bridge to the next question about guidance. You know, you raised the midpoint of guidance by 22.5 million, beat the quarter by 17.4, divide the back half of the years, should go by about 5 million. But you've closed a number of deals since last quarter's guidance.

So, can you just help me bridge, you know, the deal close versus the Philips recall? If I take a 30 percent margin on $15 million, that's a $5 million EBITDA impact or so. Is that the right way of thinking about that? Basically, I'm trying to understand what would happen to guidance if you hadn't done any acquisitions this year.

Jason Clemens
Sure. So, I'll answer the second part of that first. So, you know, in terms of the acquisition portfolio, it is very in line with the rest of the business. And so, you can think of the continued adjusted EBITDA margin that we're driving at that tell from what we reported for the quarter, that that's in line with what we're acquiring. I mean we're--you know, the numbers and what we're raising for acquisitions is right in line with the base business, if you will.

Philips, it's a little murkier. I would say, you know, we said up to 30 million of a revenue impact for the second half. You know, I don't think the number is zero, I don't think it's 30. You know, likely somewhere in between there. That's on a revenue number.

You know, we have not and we will not talk about our gross margins on that business. But, you know, even if you assumed 50 percent of that dollar dropping down--so, you know, if it's 30, 15 drops down. If it's 15, 7.5 drops down, and so on. That's the reason you're seeing the change in the margin profile. Otherwise, we're very confident that the margin profile will be just as we've said.

Pito Chickering
All right. Perfect. And then, last super quick question here, the exciting topic of DSOs. DSOs dropped very nicely, you know, in 2Q versus 1Q. Obviously, 1Q you had the acquisition--.

Jason Clemens
--Yeah--.

Pito Chickering
--Of AeroCare in there. Just curious, you know, where this exit sort--you know, of this year, there's obviously been a big, you know, questions on cash flow conversion following a short report. So, I just wanted to address both the DSOs as well as our cash flow conversion. Thanks so much, guys.

Jason Clemens
Yeah, sure. Sure, Pito. So, look, DSOs you're going to see continue in that kind of mid-40 to upper 40 range. You know, that's--we feel very comfortable there and confident there. Certainly, you're going to have a little choppiness quarter over quarter. But kind of mid-40 to high 40s on DSOs is what to expect from us.

You know, in terms of the cash flow conversion, you know, we introduced, I want to say it was Q3 of 2020, the concept of, you know, we expect to convert about two-thirds of every dollar of adjusted EBITDA into cash flow from operations. As you bridge that down to free cash flow, you know, again, we've said that capex--patient equipment capex is going to run in the ballpark of eight to 9 percent of total revenue. And then, nonpatient equipment capex is around a point or so. And so, you know, that will help you run the math on how we're thinking about free cash flow, you know, currently and going forward.

You know, so, as we stated in the prepared remarks, you know, we are right in line with that number. If you try to run that math in Q1, I think we said last quarter, it's going to be a little choppy just due to the transaction costs and the nature of Q1. But if you look at the first half of the year, we're right in line with that two-thirds of every dollar of adjusted EBITDA converting to cash flow from operations. I mean, it's the core of who we are as a company. We stay laser-focused on it, and we're very proud of it.

Pito Chickering
Great. Thanks so much. Appreciate it, guys.

Operator
Thank you. Our next question comes from Mathew Blackman with Stifel. Please proceed with your question.

Mathew Blackman
Hi. Good morning, everyone. Thanks for taking my questions. I've got a couple for Jason. This first one is a bit of a repeat of the prior question, but I want to make sure I'm thinking about the new guidance correctly.

So, you added sort of roughly 100 million--and this is sort of relative, I guess, to the last guidance range raise, but you added about roughly 100 million in M&A. You raised at the midpoint by about 130 million, and that's despite the $30 million headwind from Respironics. Is that sort of the right way to think about it? So, the underlying business looks like contributed a reasonable amount of the guidance range raise. Is that right?

Jason Clemens
Matt, that's the right way to think of it. I'd point out for you on the bottom of the range, we brought it up 165. And so, what you're seeing there is as we get later into the year, we are tightening the range. We're bringing it all up. The bottom is coming up significantly more than the top. Despite headwinds that we are expecting with Philips, you know, we feel great about the raise.

Mathew Blackman
Okay. I appreciate that. And then, Jason, another one for you. How should we think about the second half cadence? I mean, there's a lot of moving parts with potentially seasonality, delta virus, the deals you've completed, obviously, the Respironics recall, which may sort of disproportionately impact the third or the fourth quarter. Is there any way you can help us to think about a reasonable range for the third quarter, again, given all these moving parts?

Jason Clemens
Yeah. Sure, Matt. So, I'm going to reference some kind of shape and seasonality discussion we talked about last quarter. And I'm also going to reference the Q1 pro forma revenue number that I gave you of 564 because if you use the 482 that we reported, that's missing a month of AeroCare, and it's going to throw your numbers a bit.

So, in using the 564, if you just add that, you know, to our--to the top of our guide, you're going to be in that 23--22, 23 percent ballpark for Q1 for the total company and the amount of revenue that we produced as part of the annual revenue.

Again, as we said historically, you know, that's going to bump up about a point in Q2, about another point, maybe a point and a half in Q3, and then the balance of that is going to be in Q4. You should be at a 26 to 27 percent of the annual revenue will be delivered in Q4.

You know, gain, as discussed in diabetes, that is a much more pronounced slope within that book of business. Q1, you're going to be closer to an 18 percent or so and you're going to exit the year closer to about 27, 28 percent or so. So, again, just a more pronounced slope. But in terms of the overall business, that's what to expect.

Mathew Blackman
Really helpful. And then, if I could sneak one last one for Josh. You touched on all the progress being made on the sort of the cost side of AeroCare. Any update on how you're progressing on sort of the revenue synergy opportunities for AeroCare? But I guess also for Solara as well. Any update there would be helpful. Really appreciate it. Thanks.

Josh Parnes
Sure. So, I'll address the Solara revenue synergy as well. So, I think a lot of the revenue synergies that I mentioned previously that we got from our experience in resupply with a lot of these acquisitions, particularly the six on the diabetes that we've done over the last year, that's been really driving, and we believe will continue to drive organic growth in that product category.

On the AeroCare side, I think we're seeing two things. We're seeing, obviously, the cost synergies and contributing to our increased margins. But also, we're seeing really the AeroCare organic growth engine that essentially consolidated with our AdaptHealth sales efforts, which are driving organic growth across both organizations. Obviously, you know, the sales synergies, as you know, generally take a little bit longer than cost synergies, and we definitely feel like it's starting to kick into gear, you know, somewhat six months into the integration and definitely should have an impact on our late '21, '22 numbers.

Mathew Blackman
Thank you.

Operator
Thank you. Our next question comes from Kevin Fischbeck with Bank of America. Please proceed with your question.

Courtney Fondufe
Hey, guys. This is Courtney Fondufe on for Kevin. How's everyone doing? Thanks for taking the question.

Just, I guess, to reiterate a bit on the guide. Can you flesh out, you know, what does your guide really assume in terms of any COVID impact for the back half of the year? I guess, especially with, you know, the resurgence of the Delta variant, how are you thinking about that progressing through with oxygen and ventilator volumes?

Jason Clemens
Hey, Courtney. Good morning. This is Jason. You know, it is included, right? It's netted. I mean, you've got some other positive tailwinds, as well as some, you know--some headwinds that are in the revenue raise that we included. I mean, the big dollars are really from acquisitions and from the Philips numbers that we previously discussed.

But, you know, I'd say that in terms of tailwind, I mean, we did include the public health emergency extension dollars as part of this guide. You know, that will run through here for another 90 days until that will be reconsidered. You know, but that's included. That's on the positive side.

On the negative side, to your point, there are some dollars in here for COVID resurgent risk. You can think of that similar to Philips in that for balance of year, those aren't going to be huge dollars just due to the compounding effect of our business. So, you know, if there is a COVID impact in Q3, right, it would likely be slight as you miss out on resupply of those, you know, missed patients in Q4 that gets a little--could get a little bigger.

And so, we've accounted for all that. I mean, again, similar to the Philips math of what we produced. But for COVID, it's just--I can't say it's an overly material number.

Courtney Fondufe
Okay. Yeah, that's really helpful. And then, I guess one quick one on organic growth. I guess you guys mentioned that in diabetes, you feel like you're growing in line with market. I don't know if I misheard this comment, but I thought you said that specifically relating to diabetes. So, I guess, could you comment on other segments? Like, how you think the organic growth is tracking for Adapt compared to the market?

Jason Clemens
Sure. I'd say that, you know, first, when we talk about the kind of traditional DME or the--you know, we sometimes refer to that as the bent metal, you know, that's in line with our overall

end market expectations. Think of that as--you know, we've said two to 4 percent, somewhere in that ballpark, consistent with kind of any stats you'll see from CMS on aging population and elective surgeries and such.

When you get to the supplies to the home business, that's a very Steady Eddie business. I mean, that has continued to be about a two to 3 percent or so organic grower, and that's all in-line.

You know, respiratory, we saw a bit of a pop in Q1. As we spoke about previously, that was really related to kind of COVID impacts, starting around Thanksgiving through, call it, mid- to late February. But, you know, those numbers have normalized, and you're going to see that as a mid-single-digit grower.

Sleep is a touch light. I mean we've got that at seven to 9 percent is our end market expectation. It is still a little bit light, but new starts have absolutely come back. So, you know, we're still kind of filling the census, if you will, for the COVID impact in mid-2020 that I discussed in the prepared remarks.

And then diabetes, as we said, you know, we've said, you know, that the net impact of end market growth in that business line is about 10 to 12 percent, as Josh said. You know, current data, right, this quarter in particular, we're tracking against what you're hearing from others about end market growth, which is a number quite north of that. And as we get more data behind us, you should expect us to refresh those numbers.

Courtney Fondufe
Okay. Thanks, Jason.

Operator
Thank you. Our next question comes from Eric Coldwell with Baird. Please proceed with your question.

Eric Coldwell
Thanks. Good morning. I have quite a few, actually. They're all around the Philips recall.

Jason, first, it sounds like you put in a range of estimates for the impact somewhere between zero and 30. On the low end of your guidance increase, did you use the low end of the Philips impact or the high end of the Philips impact? I'm just trying to get a sense on how that played into the range.

Jason Clemens
Yeah. It's the higher, Eric. So, 30 on the bottom of the range. And I think we've got about 10 on the top. You know, I don't think it's zero. I mean, we've said up to 30. But if you unpack the acquisition raise, as well as the Philips raise, it's 30 of risk on the bottom and 10 of risk on the top.

Eric Coldwell
Great. And then, is it possible to get a sense on how that played out between 3Q and 4Q? More importantly--.

Jason Clemens
--Sure. I mean, it's--yeah, it's very back-weighted. You know, so, again, theoretically, if you--if either there's just less patients to service or if there's an impact that you don't have product to service a patient, you know, in Q3, that's going to impact your rental revenue in that quarter. But, you know, really, there would be no impact to resupply revenue for that quarter.

Eric Coldwell
Right.

Jason Clemens
As you get into Q4, you know, again, this is theoretically, you would still have potential impact in your rental revenue. But now, the Q3 patients you would have brought on census aren't there to resupply. So, resupply starts compounding in Q4. So, that's a lot of words to say it's very back weighted.

Eric Coldwell
Yeah. And then, that leads to my question on mix, which is--I guess our assumption is that the primary impact would be on equipment as long as we had good patient adherence, compliance, and not a lot of drop-offs on any new patient concerns out there. I'm curious what you can tell us about what you're seeing on resupply right now and what kind of calls you're getting to your centers or with your reps. Are you sensing patient concern or not so much?

Jason Clemens
Steve, Josh, you guys want to add to this--?

Steve Griggs
--Yeah. This is Steve. I'll take that. Surprisingly, you know, with any patient that says they stopped using their equipment, we stop billing no matter what that is, of course. And it's been surprisingly low, you know, a few hundred patients, really, that have said they've stopped using their Respironics machine.

So, I think that after the initial panic, the referral sources in health systems have, you know, contacted these patients and calmed them down and said, you know, here's some mitigation techniques that you can do to relieve some of the risk on the Respironics unit. And then hopefully, you'll get a new unit relatively soon. So, it's been very little.

And then on the resupply side, it's been also very little where you just haven't had that many patients. It's again in the hundreds that have said that they're not going to order their resupply because they're not using their machine anymore. So, the first number is on, like, you know, active rentals where we're getting rental revenue, you know, and that peels off, as you know, after 10 to 13 months when it becomes a purchased unit. And then, on the resupply as those patients after that time period. And again, it's very little.

Eric Coldwell
Yeah. And then, on the equipment versus resupply, I know you don't want to break out margin per se, but our--I guess our preconceived notion was that the equipment was low margin, and the resupply is high margin. Is that the safe approach?

Steve Griggs
Yes.

Eric Coldwell
Yeah. And then, payer discussions. With--you know, with this kind of a supply chain situation and at least in other distribution-type channels, you typically see changes in payer behavior or changes in market prices. I know this is different because a lot of it is controlled under preset contracting.

But what kind of discussions are you having with payers right now? And are you seeing any changes or potential changes in the pricing dynamics in the market given the--you know, the situation at hand?

Steve Griggs
Well, not yet, but I--but we are having discussions with them. So, you know, Medicare--CMS will announce their inflation indicator here relatively soon that will adjust our Medicare prices. And I think that's going to lead to a lot more discussion, but we're in discussion with them, but very little movement. I mean, you have some isolated things, and we've seen a Medicaid plan or two make a positive adjustment to the rates. But it's pretty insignificant to date. But we are in discussions with them and talking with them. So, not much to report yet.

Eric Coldwell
Okay. Last couple of ones. Sorry for all of this, but I--yeah, thought this was a bigger topic. So, we've heard ResMed's been giving higher allocations to large established providers in the marketplace. We've heard numbers of 20 percent, 25 percent. You may not want to quote a number, but have you been able to gain incremental allocations above historical purchasing patterns from other players in the market whether or not it's ResMed?

Steve Griggs
Well, first to ResMed, they've made it very clear, and we've agreed with this, that they are taking their customers' historic purchases, and that's where they base it. And then, they take what they're able to produce to the historical demand and that creates a percentage. That percentage was less than historical for July, and it's going to be less than historical for August.

And then, that percentage is applied to all providers regardless of size. So, you know, Adapt, Apria, Lincare, Rotec, whoever is getting the same percentage as the smallest player in the market.

As far as other suppliers, there's some that are trying to come in there, but they have such low market share. We had a few equipment manufacturers that thought they might rev it back up, but they've declined. So, right now, you know, you're obviously seeing on new patients the shortage from Philips and then historic shortage from ResMed that we hope at least they'll be able to get back to their normal demand by the end of the quarter and then hopefully increase that in the fourth quarter. So, that's what we're hoping.

But there's a national--global wide shortage of components. Intel announced that the chip shortage is real, and it's going to last for an extended period of time. So, that's in all products, not just, you know, PAP equipment.

Eric Coldwell
Yeah. Yeah. And then I guess last one--well, maybe still another. Have you had any consideration of working with some of the Chinese manufacturers that have EUAs?

Steve Griggs
Yes. Yes. We're in early, early, early discussions.

Eric Coldwell
Okay. And then last one, I promise. Unused product in the channel, product in, you know, the number of sites that you have, you've done a lot of M&A. You've probably acquired companies that had some inventory.

What have you been able to find, whether it's, you know, under the patient's bed or in their closet or in one of your facilities? Have you been able to find more supply than perhaps you thought you had or maybe some safety inventory? I'm just curious, you know, what kind of a safety net do you have at this point considering this could go on for a while?

Steve Griggs
Yeah. We're confident that inventory can help us out, you know, in the third quarter for sure and then some of the fourth quarter. And so, just really dependent on how far that inventory goes based on what ResMed can do. I just don't see new equipment coming from Respironics anytime this year.

So, I think that will squeak us through the year. But I suspect the demand is going to drop a little bit, too, as health systems start saying, okay, can we--you know, should we be even trying to get these patients into the sleep labs and try to get pieces of equipment that--or order some piece of equipment that possibly can't get? So, I think the demand side is going to be challenged also. So that's the--as we go and we learn more and more, you know, through this process, I think, you know, we'll get more information.

The FDA came out and was--had a positive statement or a better statement of how to handle this, you know, crisis. Go see your doctor and then discuss the use of your machine, versus the opposite that Philips Respironics put out, which was stop using your machine and go see the doctor.

But they still haven't given Philips the green light on the remuneration, you know, things that they want to do. So, hopefully, that's going to come out here in the next, you know, 30 to 60 days, I would hope. And then, that gives a lot more clearance and guidance on, you know, how long this is going to last.

Eric Coldwell
Okay. I appreciate all the answers. I'll leave it at that. Thanks, again.

Steve Griggs
Thanks, Eric.

Operator
Thank you. Our final question comes from Richard Close with Canaccord Genuity. Please proceed with your question.

Richard Close
Yeah, thanks. Josh, I wonder if you could talk a little bit more about that--the COPD program that you talked about. And you know, what's the opportunity with stuff like that?

Josh Parnes
Sure. Yeah. So, happy to take that. So, on the COPD program, essentially what we're doing is we're enrolling our high-end respiratory event patients in a particular part of the country on a program that really helps clinicians monitor kind of real-time outcomes, gathers that data, puts it into kind of a technology that allows us to share that data with both the clinician and the health system.

And really what, essentially, we're doing is we're tracking, you know, not just is the patient adherent to the actual therapy of the ventilator, but how they're doing kind of on a longer-term basis and how that relates to their plan of care. So, that's really kind of just early innings, let's say, of how we're thinking about chronic disease management across multiple different product categories that we believe should have real good runway on that, particularly sleep and diabetes.

So, already on sleep, we're managing and coaching patients on adherence. Our goal is to do that over a longer period of time with those patients, as well as on the diabetes side. Really, you know, we--we're working on some things with coaching on CGMs and working on how do we get that patient essentially not just adherent to the device, but really how do we get data around us being able to manage how well they're doing on their diabetes therapy and how we can be helpful to all the stakeholders within that, which is physicians, insurance companies, obviously, the customers and the patients.

But really, we sit at the intersection of being able to gather that data, but also impact that patient by leveraging the existing relationship where we have with that patient and that trusted relationship and also being able to be cost-effective at doing that at the same time without a really large investment in infrastructure to be able to do that.

So, you know, it's early innings on that, but I'd say it's something that I'm going to be focused on and I'm going to be pushing to drive that over the next couple of quarters.

Richard Close
Great. Thank you.

Operator
Thank you. Ladies and gentlemen, we have reached the end of the question-and-answer session. I will now turn the call over to Steve Griggs for closing remarks.

Steve Griggs
Thank you, and thanks to everybody for participating in your questions and your interest. We really appreciate it. And again, thanks to all of our incredible employees throughout our organization that are helping us with our continued mission to better serve our patients and improve outcomes. So, thanks a lot.

Everybody, have a great day. Thank you.

Operator
This concludes today's conference. And you may disconnect your lines at this time. Thank you for your participation and have a wonderful day.