PENNYMAC FINANCIAL SERVICES, INC.
Form POS AM
March 17, 2014

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As filed with the Securities and Exchange Commission on March 14, 2014

Registration No. 333-191522

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

POST-EFFECTIVE AMENDMENT NO. 1
TO

FORM S-1

REGISTRATION STATEMENT
Under
The Securities Act of 1933

PennyMac Financial Services, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	**6162**	**80-0882793**
(State or Other Jurisdiction of Incorporation or Organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

6101 Condor Drive
Moorpark, CA 93021
Phone: (818) 224-7442
(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

Jeffrey P. Grogin
Chief Administrative and Legal Officer and Secretary
PennyMac Financial Services, Inc.
6101 Condor Drive
Moorpark, CA 93021

Phone: (818) 224-7442

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Please send copies of all communications to:
Timothy R. Rupp
Richard J. Welch
Bingham McCutchen LLP
355 South Grand Avenue, Suite 4400
Los Angeles, CA 90071
(213) 680-6400

Approximate date of commencement of the proposed sale to the public:
From time to time after the effective date of this Registration Statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box. ý

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer o	Non-accelerated filer ý (Do not check if a smaller reporting company)	Smaller reporting company o

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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EXPLANATORY NOTE

This Post-Effective Amendment No. 1 to the Registration Statement on Form S-1 (File No. 333-191522) (the "Registration Statement") of PennyMac Financial Services, Inc. (the "Company") is being filed pursuant to the undertakings in Item 17 of the Registration Statement to update the information contained in the Registration Statement, as originally declared effective by the Securities and Exchange Commission on October 28, 2013, and to include the information contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013 (the "Annual Report") that was filed with the Securities and Exchange Commission on March 14, 2014.

The information included in this filing updates and supplements the Registration Statement and the Prospectus contained therein. No additional securities are being registered under this Post-Effective Amendment No. 1. All applicable registration fees were paid at the time of the original filing of the Registration Statement.

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The information in this prospectus is not complete and may be changed. These securities may not be sold until the post-effective amendment to the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and we are not soliciting offers to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED MARCH 14, 2014

PROSPECTUS

43,973,679 Shares

PennyMac Financial Services, Inc.

Class A Common Stock

This prospectus relates to the resale from time to time by the selling stockholders identified in this prospectus or a supplement hereto of up to 43,973,679 shares of our Class A common stock, of which 36,063,679 shares are issuable upon the exchange of Class A Units of our subsidiary Private National Mortgage Acceptance Company, LLC, or PNMAC, and 7,910,000 shares are currently held by two of the selling stockholders.

The selling stockholders may offer the shares from time to time as each selling stockholder may determine through public or private transactions or through other means described in the section entitled "Plan of Distribution" or in a supplement to this prospectus. Each selling stockholder may also sell shares under Rule 144 under the Securities Act of 1933, as amended, if available, rather than under this prospectus. The registration of these shares for resale does not necessarily mean that the selling stockholders will sell any of their shares.

We will not receive any of the proceeds from the sale of these shares by the selling stockholders.

Our Class A common stock is listed on the New York Stock Exchange, or NYSE, under the symbol "PFSI". The last reported sale price of our Class A common stock on the NYSE on March 12, 2014 was $17.78 per share.

We are an "emerging growth company" as defined in the Jumpstart Our Business Startups Act of 2012, and therefore have elected to comply with certain reduced public company reporting requirements.

We are not a government-sponsored entity.

Investing in our common stock involves risks. See "Risk Factors" beginning on page 7.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is , 2014

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ABOUT THIS PROSPECTUS

This prospectus is a part of a "shelf" registration statement on Form S-1 that we filed with the Securities and Exchange Commission, or the SEC, utilizing a continuous registration process. Under this continuous registration process, the selling stockholders may, from time to time, sell the offered securities described in this prospectus in one or more offerings. Additionally, under this shelf registration process, in certain circumstances, we may provide a prospectus supplement that will contain specific information about the terms of a particular offering by the selling stockholders. We may also provide a prospectus supplement to add information to, or update or change information contained in, this prospectus. You should read both this prospectus and any prospectus supplement, including all documents incorporated herein or therein by reference, together with additional information described under "Where You Can Find More Information" and "Information Incorporated by Reference."

Unless the context requires otherwise, the words "we," "us," "our" and "Company" refer to PennyMac Financial Services, Inc. and its subsidiaries taken as a whole. For purposes of this prospectus, the term "stockholders" shall refer to the holders of our common stock.

In this prospectus, we refer to BlackRock Mortgage Ventures, LLC, together with its affiliates, as "BlackRock," and HC Partners LLC, formerly known as Highfields Capital Investments LLC, together with its affiliates, as "Highfields."

Unless the context requires otherwise, references in this prospectus to "PMT" collectively refer to PennyMac Mortgage Investment Trust, a mortgage "real estate investment trust" externally managed by PCM, and its operating subsidiaries.

You should rely only on the information contained in this prospectus or contained in any prospectus supplement or free writing prospectus filed with the Securities and Exchange Commission, or SEC. Neither we nor the selling stockholders have authorized anyone to provide you with additional information or information different from that contained in this prospectus or in any prospectus supplement or free writing prospectus filed with the SEC. This prospectus does not constitute an offer to sell, or solicitation of an offer to buy, these securities in any jurisdiction where such offer, sale or solicitation is not permitted. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospects may have changed since that date.

For investors outside the United States: We have not done anything that would permit this offering or possession or distribution of this prospectus in any jurisdiction where action for that purpose is required, other than in the United States. You are required to inform yourselves about and to observe any restrictions relating to this offering and the distribution of this prospectus outside of the United States.

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SUMMARY

Our Company:

We are a specialty financial services firm with a comprehensive mortgage platform and integrated business focused on the production and servicing of U.S. residential mortgage loans and the management of investments related to the U.S. residential mortgage market. We were founded in 2008 by members of our executive leadership team and two strategic partners, BlackRock and Highfields. Since our founding we have pursued opportunities to acquire and manage residential mortgage loans and established what we believe to be a best-in-class mortgage platform. We have relied on the know-how of our management team and built a *de novo* operating platform to our specifications using industry-leading technology, processes and procedures to address the stringent requirements of residential mortgage lending and servicing in the post-financial crisis market. We believe that this approach has resulted in a specialized mortgage platform that is "legacy-free" and highly scalable to support the continued growth of our business.

We conduct our business in two segments: mortgage banking and investment management. Our principal mortgage banking subsidiary, PennyMac Loan Services, LLC, or PLS, is a leading non-bank producer and servicer of mortgage loans in the United States. PLS is a seller/servicer for the Federal National Mortgage Association, or Fannie Mae, and the Federal Home Loan Mortgage Corporation, or Freddie Mac, each of which is a government-sponsored entity, or GSE. It is also an approved issuer of securities guaranteed by the Government National Mortgage Association, or Ginnie Mae, a lender of the Federal Housing Administration, or FHA, a lender/servicer of the Veterans Administration, or VA, and a servicer for the Home Affordable Modification Program, or HAMP. PLS is licensed (or exempt or otherwise not required to be licensed) to originate residential mortgage loans in 47 states and the District of Columbia and to service loans in 49 states, the District of Columbia and the U.S. Virgin Islands.

Our principal investment management subsidiary, PNMAC Capital Management, LLC, or PCM, is an SEC registered investment adviser. It manages PennyMac Mortgage Investment Trust, or PMT, a mortgage "real estate investment trust," or REIT, listed on the NYSE. PCM also manages PNMAC Mortgage Opportunity Fund, LLC and PNMAC Mortgage Opportunity Fund, LP, both registered under the Investment Company Act of 1940, an affiliate of these funds and PNMAC Mortgage Opportunity Fund Investors, LLC. We refer to these funds collectively as our "Investment Funds" and, together with PMT, as our "Advised Entities." Our Advised Entities have been some of the leading non-bank investors in distressed mortgage loans since 2008, investing in loans with approximately $7.4 billion of unpaid principal balances, or UPB. As of December 31, 2013, our Advised Entities had combined net assets of approximately $2.0 billion.

We conduct some of our activities for our own account and some for our Advised Entities. We earn significant fee income and carried interest from the activities we conduct for our Advised Entities; such fees include investment management fees, incentive fees, subservicing fees for servicing loan portfolios and fulfillment fees for mortgage banking services provided to PMT in connection with our correspondent lending program. Our relationships with our Advised Entities also allow us to pursue some market opportunities with reduced capital intensity, with PLS and PCM providing operational expertise and our Advised Entities providing investment capital for mortgage-related assets.

Corporate and Other Information:

PNMAC was formed in Delaware in January 2008. PennyMac Financial Services, Inc. was formed in Delaware in December 2012. Our principal executive offices are located at 6101 Condor Drive in Moorpark, California and our telephone number is (818) 224-7442. Our website address is www.IR.PennyMacFinancial.com. We do not incorporate the information contained on, or accessible

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through, our corporate website into this prospectus, and you should not consider it part of this prospectus.

We are an "emerging growth company" as defined in the Jumpstart Our Business Startups Act of 2012. We will remain an emerging growth company until the earlier of (1) the last day of the fiscal year (a) following the fifth anniversary of the completion of the initial public offering of our Class A common stock on May 9, 2013, (b) in which we have total annual gross revenue of at least $1.0 billion, or (c) in which we are deemed to be a large accelerated filer, which means the market value of our Class A common stock that is held by non-affiliates exceeds $700 million as of the prior June 30th, and (2) the date on which we have issued more than $1.0 billion in non-convertible debt securities during the prior three-year period. We refer to the Jumpstart Our Business Startups Act of 2012 in this prospectus as the "JOBS Act," and references in this prospectus to "emerging growth company" shall have the meaning ascribed to it in the JOBS Act.

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THE OFFERING

Class A common stock to be offered by the selling stockholders	Up to 43,973,679 shares, of which 36,063,679 shares are issuable by us to the selling stockholders upon the exchange of Class A Units of PNMAC on a one-for-one basis (subject to the customary conversion rate adjustments described below).
Class A common stock outstanding after giving effect to this offering	56,943,165 shares, assuming the exchange of 36,063,679 Class A Units of PNMAC for an equivalent number of shares of our Class A common stock.
Class A Units of PNMAC outstanding after giving effect to this offering	18,945,723 units held by the members of PNMAC other than PennyMac Financial Services, Inc. and 56,943,165 units held by PennyMac Financial Services, Inc., assuming the exchange of 36,063,679 Class A Units of PNMAC for an equivalent number of shares of our Class A common stock.
Voting power held by holders of Class A common stock after giving effect to this offering	75.03%, assuming the exchange of 36,063,679 Class A Units of PNMAC for an equivalent number of shares of our Class A common stock. The remaining voting power is held by holders of our Class B common stock.
Voting rights	Each share of our Class A common stock entitles its holder to one vote on all matters to be voted on by stockholders generally. Each holder of Class A Units of PNMAC, other than PennyMac Financial Services, Inc., holds one share of our Class B common stock. The shares of Class B common stock have no economic rights but entitle the holder, without regard to the number of shares of Class B common stock held, to a number of votes on matters presented to stockholders of PennyMac Financial Services, Inc. that is equal to the aggregate number of Class A Units of PNMAC held by such holder. See "Description of Capital Stock Common Stock Class B Common Stock." Holders of our Class A common stock and Class B common stock vote together as a single class on all matters presented to our stockholders for their vote or approval, except as otherwise required by applicable law.

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Exchange rights of holders of Class A Units of PNMAC	Pursuant to an exchange agreement that we have entered into with the owners of PNMAC other than us, those other owners may (subject to the terms of the exchange agreement) exchange their Class A Units of PNMAC for shares of Class A common stock of PennyMac Financial Services, Inc. on a one-for-one basis, subject to customary conversion rate adjustments for stock splits, stock dividends, reclassifications and certain other transactions that would cause the number of outstanding shares of Class A common stock to be different than the number of Class A Units of PNMAC owned by PennyMac Financial Services, Inc. As those other owners exchange Class A Units of PNMAC for shares of Class A common stock, the voting power afforded to them by their shares of Class B common stock will be automatically and correspondingly reduced. We have also entered into a tax receivable agreement with certain of the owners of PNMAC other than us that will provide for the payment by PennyMac Financial Services, Inc. to those other owners of 85% of the tax benefits, if any, that PennyMac Financial Services, Inc. is deemed to realize under certain circumstances as a result of (i) increases in tax basis resulting from exchanges of Class A Units of PNMAC and (ii) certain other tax benefits related to our entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement.
Use of proceeds	We will not receive any proceeds from the sale of shares of our Class A common stock by the selling stockholders. The selling stockholders will receive all of the net proceeds and bear all commissions and discounts, if any, from the sales of our Class A common stock offered by them pursuant to this prospectus.
Dividend policy	Any future determination to pay dividends on our common stock will be at the discretion of our board of directors and will depend upon many factors, including our financial position, results of operations, liquidity and legal requirements.
Risk factors	See "Risk Factors" beginning on page 7 and the other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in our Class A common stock.
NYSE symbol	"PFSI."

Unless we specifically state otherwise, all information in this prospectus:

- reflects the 20,879,486 shares of Class A common stock and 75,888,888 Class A Units of PNMAC (including 20,879,486 Class A Units owned by PennyMac Financial Services, Inc.) outstanding as of March 12, 2014;

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- does not reflect options to purchase 414,349 shares of Class A common stock outstanding as of March 12, 2014, at a weighted average exercise price of $21.03 per share, none of which are currently vested or exercisable, or 584,661 outstanding restricted stock units as of March 12, 2014 to obtain up to 584,661 shares of Class A common stock, none of which are currently vested or exercisable;

- does not reflect an additional 4,229,447 shares of Class A common stock that may be granted as of March 12, 2014 under the PennyMac Financial Services, Inc. 2013 Equity Incentive Plan, referred to in this prospectus as our 2013 Equity Incentive Plan, which number represents the total number of additional shares currently authorized and reserved for issuance in connection with future awards that may be granted under this plan less the number of shares issuable under this plan in exchange for Class A Units of PNMAC held by our employees pursuant to the exchange agreement; and

- does not reflect an additional 18,945,723 shares of Class A common stock issuable as of March 12, 2014 under our 2013 Equity Incentive Plan upon the exchange of Class A Units of PNMAC held by our employees pursuant to the exchange agreement.

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RISK FACTORS

Investment in any securities offered pursuant to this prospectus involves risks. You should carefully consider the specific risks set forth under "Risk Factors" in Item 1A of Part I of our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 incorporated by reference herein, and all of the other information contained or incorporated by reference in this prospectus, before making an investment decision. For more information, see "Information Incorporated by Reference."

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements, which reflect our current views with respect to, among other things, our operations and financial performance. You can identify these forward- looking statements by the use of words such as "outlook," "believes," "expects," "potential," "continues," "may," "will," "should," "seeks," "approximately," "predicts," "intends," "plans," "estimates," "anticipates" or the negative version of these words or other comparable words. Such forward-looking statements are subject to various risks and uncertainties. Accordingly, there are or will be important factors that could cause actual outcomes or results to differ materially from those indicated in these statements. We believe these factors include but are not limited to those described under "Risk Factors" and include, among other things:

The continually changing federal, state and local laws and regulations applicable to the highly regulated industry in which we operate;

Lawsuits or governmental actions if we do not comply with the laws and regulations applicable to our businesses;

The creation of the Consumer Finance Protection Bureau, or CFPB, its recently issued and future rules and the enforcement thereof by the CFPB;

Changes in existing U.S. government-sponsored entities, their current roles or their guarantees or guidelines;

Changes to government mortgage modification programs;

The licensing and operational requirements of states and other jurisdictions applicable to our businesses, to which our bank competitors are not subject;

Foreclosure delays and changes in foreclosure practices;

Certain banking regulations that may limit our business activities;

Changes in macroeconomic and U.S. residential real estate market conditions;

Difficulties inherent in growing loan production volume;

Changes in prevailing interest rates;

Difficulties inherent in adjusting the size of our operations to reflect changes in business level;

Purchase opportunities for mortgage servicing rights, or MSRs, and our success in winning bids;

Increases in loan delinquencies and defaults;

Our reliance on PMT as a significant source of financing for, and revenue related to, our mortgage banking business;

Any required additional capital and liquidity to support business growth that may not be available on acceptable terms, if at all;

Our obligation to indemnify third-party purchasers or repurchase loans if loans that we originate, acquire or assist in the fulfillment of, fail to meet certain criteria or characteristics or under other circumstances;

Our obligation to indemnify PMT and the Investment Funds if our services fail to meet certain criteria or characteristics or under other circumstances;

Decreases in the historical returns on the assets that we select and manage for our clients, and our resulting management and incentive fees;

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- The extensive amount of regulation applicable to our investment management segment;
- Conflicts of interest in allocating our services and investment opportunities among ourselves and our Advised Entities;
- The potential damage to our reputation and adverse impact to our business resulting from the ongoing negative publicity focused on Countrywide Financial Corporation, given the former association of certain of our officers with that entity; and
- Our recent rapid growth.

These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this prospectus. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

MARKET DATA

This prospectus includes market and industry data and forecasts that we have derived from independent consultant reports, publicly available information, various industry publications, other published industry sources and our internal data and estimates. Independent consultant reports, industry publications and other published industry sources generally indicate that the information contained therein was obtained from sources believed to be reliable.

Our internal data and estimates are based upon information obtained from trade and business organizations and other contacts in the markets in which we operate and our management's understanding of industry conditions. Although we believe that such information is reliable, we have not had this information verified by any independent sources.

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ORGANIZATIONAL STRUCTURE

The diagram below depicts our organizational structure as of March 14, 2014 and without giving effect to any exchanges by the selling stockholders and subsequent sales of shares of Class A common stock in this offering.

PennyMac Financial Services, Inc. is the sole managing member of PNMAC and, through PNMAC and its subsidiaries, operates our business. Accordingly, although PennyMac Financial Services, Inc. currently has a minority economic interest in PNMAC, PennyMac Financial Services, Inc. has 100% of the voting power and controls the management of PNMAC, subject to certain exceptions. See "Certain Relationships and Related Party Transactions PNMAC Limited Liability Company Agreement."

(1) Excluding Fidelity Investments Charitable Gift Fund, which has exchanged all of its Class A Units for shares of Class A common stock.

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Reorganization and Recapitalization

Prior to, and in connection with, the initial public offering of our Class A common stock, the limited liability company agreement of PNMAC was amended and restated to, among other things, modify the capital structure of PNMAC by converting all existing classes of limited liability company units into Class A Units. The allocation of Class A Units among our then-existing owners was determined pursuant to the distribution provisions of the limited liability company agreement of PNMAC prior to that amendment and restatement based upon the liquidation value of PNMAC, assuming that it was liquidated at the time of our initial public offering with a value implied by the $18.00 per share price of the shares of Class A common stock sold in our initial public offering. Immediately following this reorganization but prior to the completion of our initial public offering, there were 63,111,111 Class A Units issued and outstanding.

Upon the completion of our initial public offering, PennyMac Financial Services, Inc. purchased 12,777,777 newly issued Class A Units from PNMAC at a purchase price per unit equal to the initial public offering price per share of our Class A common stock less the underwriting discount per share. This number of newly issued Class A Units equaled the number of shares of Class A common stock sold in our initial public offering and the price paid by PennyMac Financial Services, Inc. for the purchase of those Class A Units constituted the entire amount of net proceeds that it received from our initial public offering.

We refer to the foregoing transactions, collectively, as the "Recapitalization."

Following our initial public offering of our Class A common stock, the selling stockholders retained their equity ownership in PNMAC, an entity that is intended to be classified as a partnership for United States federal income tax purposes (and not as an association, taxable mortgage pool or publicly traded partnership, each of which could be taxable as a corporation), in the form of Class A Units of PNMAC. Investors in this offering will, by contrast, hold their equity ownership in PennyMac Financial Services, Inc., a Delaware corporation that is a domestic corporation for United States federal income tax purposes, in the form of shares of Class A common stock. We believe that the selling stockholders generally find it advantageous to hold their equity interests in an entity that is not taxable as a corporation for United States federal income tax purposes. The selling stockholders and PennyMac Financial Services, Inc. currently incur U.S. federal, state and local income taxes on their proportionate share of any taxable income of PNMAC. We do not believe that our organizational structure gives rise to any significant benefit or detriment to our business or operations.

We have entered into an exchange agreement with the owners of PNMAC other than us. Under the exchange agreement, the other owners of PNMAC (and certain permitted transferees thereof) may elect or, under certain circumstances, are obligated (subject to the terms of the exchange agreement) to exchange their Class A Units of PNMAC for shares of Class A common stock of PennyMac Financial Services, Inc. on a one-for-one basis, subject to customary conversion rate adjustments for stock splits, stock dividends, reclassifications and certain other transactions that would cause the number of outstanding shares of Class A common stock to be different than the number of Class A Units of PNMAC owned by PennyMac Financial Services, Inc. As a holder exchanges its Class A Units of PNMAC, PennyMac Financial Services, Inc.'s interest in PNMAC is correspondingly increased. See "Certain Relationships and Related Party Transactions Exchange Agreement."

These exchanges are expected to result in increases in the tax basis of the assets of PNMAC that otherwise would not have been available. These increases in tax basis may reduce the amount of tax that PennyMac Financial Services, Inc. would otherwise be required to pay in the future. These increases in tax basis may also decrease gains (or increase losses) on future dispositions of certain capital assets to the extent tax basis is allocated to those capital assets. We have entered into a tax receivable agreement with the owners of PNMAC other than us that will provide for the payment by PennyMac Financial Services, Inc. to those owners of 85% of the amount of the benefits, if any, that

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PennyMac Financial Services, Inc. is deemed to realize as a result of (i) increases in tax basis resulting from exchanges of Class A Units of PNMAC and (ii) certain other tax benefits related to our entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement. These payment obligations are obligations of PennyMac Financial Services, Inc. and not of PNMAC. PennyMac Financial Services, Inc. and its stockholders will retain the remaining 15% of the those tax benefits that PennyMac Financial Services, Inc. is deemed to realize.

All owners of PNMAC other than PennyMac Financial Services, Inc. also hold shares of Class B common stock of PennyMac Financial Services, Inc. Although these shares have no economic rights, they allow those owners of PNMAC to exercise voting power at PennyMac Financial Services, Inc., the managing member of PNMAC, at a level that is consistent with their overall equity ownership of our business. Under our certificate of incorporation , each holder of Class B common stock is entitled, without regard to the number of shares of Class B common stock held by that holder, to one vote for each Class A Unit of PNMAC held by such holder. Accordingly, as the selling stockholders and other owners of PNMAC exchange Class A Units of PNMAC for shares of Class A common stock of PennyMac Financial Services, Inc. pursuant to the exchange agreement, the voting power afforded to them by their shares of Class B common stock is automatically and correspondingly reduced.

PennyMac Financial Services, Inc. is a holding company, and its sole material asset is its equity interest in PNMAC. As the sole managing member of PNMAC, PennyMac Financial Services, Inc. will operate and control all of the business and affairs of PNMAC and, through PNMAC and its subsidiaries, conduct our business.

We consolidate the financial results of PNMAC and its subsidiaries, and the ownership interest of the other members of PNMAC are reflected as a non-controlling interest in PennyMac Financial Services, Inc.'s consolidated financial statements.

Pursuant to the limited liability company agreement of PNMAC, PennyMac Financial Services, Inc. has the right to determine when distributions will be made to the members of PNMAC and the amount of any such distributions, other than with respect to tax distributions as described below. If PennyMac Financial Services, Inc. authorizes a distribution, such distribution will be made to the members of PNMAC, including PennyMac Financial Services, Inc., pro rata in accordance with the percentages of their respective limited liability company interests.

The holders of limited liability company interests in PNMAC, including PennyMac Financial Services, Inc., will incur U.S. federal, state and local income taxes on their proportionate share of any taxable income of PNMAC. The limited liability company agreement provides for quarterly cash distributions to the holders of limited liability company interests of PNMAC if PennyMac Financial Services, Inc. determines that the taxable income of PNMAC will give rise to taxable income for its members. In accordance with the limited liability company agreement, we are required to cause PNMAC to make quarterly cash distributions to the holders of limited liability company interests of PNMAC for purposes of funding their tax obligations in respect of the income of PNMAC that is allocated to them. Generally, these tax distributions will be computed based on the taxable income of PNMAC multiplied by an assumed tax rate determined by us.

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USE OF PROCEEDS

The selling stockholders will receive all of the net proceeds from the sales of shares of Class A common stock offered by them pursuant to this prospectus. We will not receive any proceeds from the sale of these shares of our Class A common stock, but we will bear the costs associated with this registration. The selling stockholders will bear any underwriting commissions and discounts attributable to their sale of shares of our Class A common stock.

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UNAUDITED PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The unaudited pro forma condensed consolidated statements of income for the year ended December 31, 2013 present our consolidated results of operations giving pro forma effect to the Recapitalization described under "Organizational Structure" and the acquisition of PennyMac Financial Services, Inc. Class A common shares initial public offering of our Class A common stock as if such transactions occurred on January 1, 2013. The pro forma adjustments are based on available information and upon assumptions that our management believes are reasonable in order to reflect, on a pro forma basis, the impact of these transactions on the historical financial information of PennyMac Financial Services, Inc.

Any potential future exchanges of PNMAC units for our Class A common shares have not been presented herein to reflect a pro forma basis impact on the historical financial information of PennyMac Financial Services, Inc. for the the year ended December 31, 2013 because such exchanges are not currently probable of occurring. The unaudited pro forma consolidated financial information should be read together with "Organizational Structure," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the historical financial statements and related notes included elsewhere in this prospectus or in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 incorporated by reference herein.

The unaudited pro forma consolidated financial information is included for informational purposes only and does not purport to reflect the results of operations of PennyMac Financial Services, Inc. that would have occurred had we operated as a public company during the entire period presented. The unaudited pro forma consolidated financial information should not be relied upon as being indicative of our results of operations or financial position had the Recapitalization described under "Organizational Structure" and the use of the net proceeds from our initial public offering or the potential future exchanges occurred on the dates assumed. The unaudited pro forma consolidated financial information also does not project our results of operations or financial position for any future period or date.

The pro forma adjustments principally give effect to:

- the purchase by PennyMac Financial Services, Inc. of 12,777,777 Class A Units of PNMAC in our initial public offering as if it occurred on January 1, 2013.

- A provision for corporate income taxes on the income attributable to PennyMac Financial Services, Inc. at an effective rate of 42%, which includes a provision for U.S. federal income taxes and assumes the highest statutory rates apportioned to each state and local jurisdiction.

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PENNYMAC FINANCIAL SERVICES, INC.

UNAUDITED PRO FORMA CONDENSED CONSOLIDATED STATEMENTS OF INCOME

FOR THE YEAR ENDED DECEMBER 31, 2013

	PennyMac Financial Services, Inc. Actual	Pro Forma Adjustments(1)	PennyMac Financial Services, Inc. Pro Forma
		(in thousands)	
Revenue			
Net gains on mortgage loans held for sale at fair value	$ 138,013		$ 138,013
Loan origination fees	23,575		23,575
Fulfillment fees from PennyMac Mortgage Investment Trust	79,712		79,712
Net servicing income fees:			
Loan servicing fees			
From non-affiliates	61,523		61,523
From PennyMac Mortgage Investment Trust	39,413		39,413
From Investment Funds	7,799		7,799
Mortgage servicing rebate (to) from Investment Funds	(700)		(700)
Ancillary and other fees	11,426		11,426
	119,461		119,461
Amortization, impairment and change in estimated fair value of mortgage servicing rights	(29,451)		(29,451)
Net loan servicing income	90,010		90,010
Management fees:			
From PennyMac Mortgage Investment Trust	32,410		32,410
From Investment Funds	7,920		7,920
	40,330		40,330
Carried Interest from Investment Funds	13,419		13,419
Net interest expense:			
Interest income	15,632		15,632
Interest expense:	16,673		16,673
	(1,041)		(1,041)

Goodwill and Intangible Assets

Goodwill and other intangible assets with indefinite lives are reviewed annually for impairment or more frequently if circumstances indicate impairment may have occurred.

The Company estimates the fair value of its identified reporting units and compares those estimates against the related carrying value. For each of the reporting units, the estimated fair value is determined based on a multiple of earnings before interest, taxes, depreciation, and amortization or on the estimated fair value of assets in situations when it is readily determinable.

Included in intangible assets, net are other intangible assets such as licenses to operate home-based and/or facility-based services and trade names. The Company has valued these intangible assets separately from goodwill for each acquisition completed after January 1, 2006. The Company has concluded that these licenses and trade names have indefinite lives, as management has determined that there are no legal, regulatory, contractual, economic or other factors that would limit the useful life of these intangible assets and the Company intends to renew and operate the licenses and use these trade names indefinitely. Prior to January 1, 2006, the Company elected to recognize the fair value of indefinite-lived licenses and trade names together with goodwill as a single asset for financial reporting purposes.

Components of the Company s home nursing operating segment are generally represented by individual subsidiaries or joint ventures with individual licenses to conduct specific operations within geographic markets as limited by the terms of each license. Components of the Company s facility-based services are represented by individual operating entities. Effective January 1, 2004, management aggregates the components of these two segments into two reporting units for purposes of evaluating impairment.

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Other Significant Accounting Policies

Due to/from Governmental Entities

The Company s critical access hospital and long-term acute care hospitals are reimbursed for certain activities based on tentative rates. Final reimbursement is determined based on submission of annual cost reports and audits by the fiscal intermediary. Adjustments are accrued on an estimated basis in the period the related services are rendered and further adjusted as final settlements are determined. These adjustments are accounted for as changes in estimates. There have been no significant changes in estimates during the three months ended June 30, 2007 and 2006.

Property, Building, and Equipment

Property, building, and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the individual assets, generally ranging from three to ten years and up to thirty-nine years on buildings. Depreciation expense for the three months ended June 30, 2007 and 2006 was $759,000 and $570,000 respectively. Depreciation expense for the six months ended June 30, 2007 and 2006 was $1.4 million and $1.1 million, respectively.

Capital leases are included in equipment. Capital leases are recorded at the present value of the future rentals at lease inception and are amortized over the shorter of the applicable lease term or the useful life of the equipment. Amortization of assets under the capital lease obligations is included in depreciation and amortization expense.

Long-Lived Assets

The Company reviews the recoverability of long-lived assets whenever events or circumstances occur which indicate recorded costs may not be recoverable. If the expected future cash flows (undiscounted) are less than the carrying amount of such assets, the Company recognizes an impairment loss for the difference between the carrying amount of the assets and their estimated fair value.

Income Taxes

The Company accounts for income taxes using the liability method. Under the liability method, deferred taxes are determined based on differences between the financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax laws that will be in effect when the differences are expected to reverse. Management provides a valuation allowance for any net deferred tax assets when it is more likely than not that a portion of such net deferred tax assets will not be recovered.

Minority Interest and Cooperative Endeavor Agreements

The interest held by third parties in subsidiaries owned or controlled by the Company is reported on the consolidated balance sheets as minority interest. Minority interest reported in the consolidated statements of income reflects the respective interests in the income or loss of the subsidiaries attributable to the other parties, the effect of which is removed from the Company s consolidated results of operations.

Several of the Company s home health agencies have cooperative endeavor agreements with third parties that allow the third parties to be paid or recover a fee based on the profits or losses of the respective agencies. The Company accrues for the settlement of the third party s profits or losses during the period the amounts are earned. Under the agreements, the Company has incurred net amounts due to the third parties of $65,000 and $55,000 for the three months ended June 30, 2007 and 2006, respectively, and $121,000 and $120,000 for the six months ended June 30, 2007 and 2006, respectively. The cooperative endeavor agreements have terms expiring at the end of June 2008.

For agreements where the third party is a healthcare institution, the agreements typically require the Company to lease building and equipment and receive housekeeping and maintenance from the healthcare institutions. Ancillary services related to these arrangements are also typically provided by the healthcare institution. The Company expenses these amounts as incurred.

Minority Interest Subject to Exchange Contracts and/or Put Options

The Company has a put option agreement with the minority interest holders of a majority-owned subsidiary, St. Landry Extended Care Hospital, LLC (St. Landry), which allows the minority interest holders to redeem their minority interests for cash. As of June 30, 2007, approximately 76.5% of the doctors have converted their minority interests to cash.

There were no redemptions in the six months ended June 30, 2007. In the six months ended June 30, 2007, the Company recorded a mark-to-market charge of $156,000 for these redeemable minority interests. Included in minority interests subject to exchange contracts and/or put options liability at June 30, 2007 and December 31, 2006 is $155,000 and $317,000, respectively, related to these redeemable minority interests.

Stock-based Compensation

The Company has two stock option plans that are administered by the Compensation Committee of the Board of Directors, which selects persons eligible to receive awards and determines the number of shares and/or options subject to each award, the terms, conditions, performance measures and other provisions of the award. Readers should refer to Note 6 of the Company s consolidated financial statements in its Annual Report on Form 10-K for the year ended December 31, 2006 for additional information related to these stock-based compensation plans.

The Company accounts for its stock-based compensation plans using the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123(R) (revised 2004), *Share-Based Payment*, a revision of SFAS No. 123, *Accounting for Stock-Based Compensation*.

Earnings Per Share

Basic per share information is computed by dividing the relevant amounts from the Consolidated Statements of Income by the weighted-average number of shares outstanding during the period. Diluted per share information is computed by dividing the relevant amounts from the Consolidated Statements of Income by the weighted-average number of shares outstanding plus dilutive potential shares.

The following table sets forth shares used in the computation of basic and diluted per share information:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Weighted average number of shares outstanding for basic per share calculation	17,754,632	16,561,398	17,751,412	16,559,623
Effect of dilutive potential shares:				
Options	7,871	1,454	7,856	1,197
Restricted stock	36,449	13,216	54,127	8,907
Adjusted weighted average shares for diluted per share calculation	17,798,952	16,576,068	17,813,395	16,569,727

Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157), which defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States (GAAP) and expands disclosures about fair value measurements. SFAS No. 157 will be effective for financial statements issued for fiscal years beginning after

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November 15, 2007, and interim periods within those fiscal years. The adoption of SFAS No. 157 is not expected to have a material effect on the Company s consolidated financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment to FASB Statement No. 115* (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007. The adoption of SFAS No. 159 is not expected to have a material effect on the Company s consolidated financial position or results of operations.

3. Acquisitions and Divestitures

The following acquisitions were completed pursuant to the Company s strategy of becoming the leading provider of post-acute healthcare services to Medicare patients in selected rural markets in the southern United States. The purchase price of each acquisition was determined based on the Company s analysis of comparable acquisitions and target market s potential cash flows. Goodwill generated from the acquisitions was recognized based on the expected contributions of each acquisition to the overall corporate strategy. The Company expects the goodwill recognized in connection with the acquisition of existing operations to be fully tax deductible.

2007 Acquisitions

During the six month period ended June 30, 2007, the Company acquired the existing operations of twelve entities for $8.5 million in cash and $908,000 in acquisition costs. Goodwill of $8.2 million and other intangibles of $1.3 million were assigned to the home-based services segment. The allocation of the purchase price to certain acquisitions during the six months ended June 30, 2007 has not been finalized and subject to change upon completion of final valuation.

2007 Divestitures

The Company has reclassified the operations of one long-term acute care hospital out of discontinued operations in the three months and six months ended June 30, 2007 and 2006. In the first quarter of 2007, the Company reclassified the operations of one long-term acute care hospital out of discontinued operations and the Company no longer holds the assets for sale. The facility had previously been identified as held for sale and accounted for in discontinued operations throughout the year ended December 31, 2006. Goodwill of $401,000 and other assets related to this hospital were classified as assets held for sale at December 31, 2006. The operating results for the three months and six months ended June 30, 2006, previously disclosed in discontinued operations, have been reclassified to continuing operations in the statement of income.

The Company has identified one pharmacy operation and one critical access hospital as held for sale as of June 30, 2007. The assets related to these operations are classified as assets held for sale on the balance sheet and operations are reported as discontinued operations. On July 1, 2007, the Company sold the assets of the critical access hospital to a third party.

The following table summarizes the operating results of divestitures which have been presented as loss from discontinued operations in the accompanying consolidated statements of income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Net service revenue	$ 1,000	$ 1,273	$ 2,066	$ 3,542
Costs, expenses and minority interest and cooperative endeavor allocations	1,551	1,710	3,045	4,407
Loss from discontinued operations before income tax benefit	551	437	979	865
Income tax benefit	215	166	382	329
Loss from discontinued operations	$ 336	$ 271	$ 597	$ 536

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The changes in recorded goodwill by segment for the six month period ended June 30, 2007 were as follows:

		Six months Ended June 30, 2007 (in thousands)
Home-based services segment:		
Balance at December 31, 2006	$	35,740
Goodwill acquired during the period from acquisitions		8,237
Balance at June 30, 2007	$	43,977
Facility-based services segment:		
Balance at December 31, 2006	$	3,941
Goodwill reclassified from held for sale during the period		401
Balance at June 30, 2007	$	4,342

The above transactions were considered to be immaterial individually and in the aggregate. Accordingly, no supplemental pro forma information is required.

4. Credit Arrangements

Long-Term Debt

Long-term debt consisted of the following:

	June 30, 2007		December 31, 2006
	(in thousands)		
Notes payable:			
Due in yearly installments of $50,000 through August 2010 at 6.25%	$ 200	$	190
Due in monthly installments of $20,565 through October 2015 at LIBOR plus 225 basis points (7.65% at June 30, 2007)	2,883		2,898
Due in monthly installments of $12,500 through November 2009 at 3.08%	327		391
	3,410		3,479
Less current portion of long-term debt	431		428
	$ 2,979	$	3,051

In August 2005, the Company entered into a promissory note with the seller of A-1 Nursing Registry, Inc. (A-1) in conjunction with the purchase of the assets of A-1. The principal amount of the note is $250,000 and it bears interest at 6.25%.

In August 2005, the Company entered into a promissory note with Bancorp Equipment Finance, Inc. to purchase an airplane, for a principal amount of $2,975,000 with interest on any outstanding principal balance at the one month LIBOR rate plus 225 basis points (7.65% at June 30, 2007). The note is collateralized by the Company s airplane and is payable in 119 monthly installments of $20,565 followed by one balloon installment in the amount of $1,920,565.

Certain of the Company s loan agreements contain restrictive covenants, including limitations on indebtedness and the maintenance of certain financial ratios. At June 30, 2007 and December 31, 2006, the Company was in compliance with all covenants.

Other Credit Arrangements

The Company maintains a revolving-debt arrangement. Under the terms of this arrangement, the Company may be advanced funds up to a defined limit of eligible accounts receivable not to exceed the borrowing limit. At June 30, 2007 and December 31, 2006, the borrowing limit was $22,500,000, and no amounts were outstanding. Interest accrues on any outstanding amounts at a varying rate and is based on the Wells Fargo Bank, N.A. prime rate plus 1.5% (9.75% at June 30, 2007). The annual facility fee is 0.5% of the total availability. The agreement expires on April 15, 2010.

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5. Income Taxes

The Company adopted the provisions of FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48) effective January 1, 2007. The adoption did not have a material effect on the consolidated financial position or results of operations of the Company. At the date of adoption, the Company had no unrecognized tax benefits. The Company recognizes interest and penalties related to uncertain tax positions in interest expense and general and administrative expenses, respectively. As of June 30, 2007, there were no accrued interest or penalties relating to unrecognized income tax benefits recognized in the statement of operations. There was no accrued liability for interest or penalties related to unrecognized income tax benefits recognized in the statement of financial position at June 30, 2007.

The Company is subject to both federal and state income tax for jurisdictions within which it operates. Within these jurisdictions, the Company is open to examination for tax years ended after December 31, 2002.

6. Stockholders Equity

The following table summarizes the activity in stockholders equity for the six month period ended June 30, 2007 (amounts in thousands, except share data):

	Common Stock				Additional		
	Issued		Treasury		Paid-In	Retained	
	Amount	Shares	Amount	Shares	Capital	Earnings	Total
Balances at December 31, 2006	$ 177	20,682,317	$ (2,856)	2,950,059	$ 80,273	$ 44,295	$ 121,889
Net income						10,824	10,824
Options exercised		527					
Issuance of 1,167 shares of vested restricted stock		1,167			33		33
Nonvested stock compensation					548		548
Issuance of vested restricted stock		22,476					
Excess tax benefits from issuance of nonvested stock					89		89
Issuance of common stock under Employee Stock Purchase Plan		5,995			173		173
Recording minority interest in joint venture at redemption value						156	156
Balances at June 30, 2007	$ 177	20,712,482	$ (2,856)	2,950,059	$ 81,116	$ 55,275	$ 133,712

Share Based Compensation

On January 20, 2005, the board of directors and stockholders of the Company approved the 2005 Long Term Incentive Plan (the Incentive Plan). The Incentive Plan provides for 1,000,000 shares of common stock that may be issued or transferred pursuant to awards made under the plan. A variety of discretionary awards for employees, officers, directors and consultants are authorized under the Incentive Plan, including incentive or non-qualified statutory stock options and restricted stock. All awards must be evidenced by a written award certificate which will include the provisions specified by the compensation committee of the board of directors. The compensation committee will determine the exercise price for non-statutory stock options. The exercise price for any option cannot be less than the fair market value of our common stock as of the date of grant.

Also on January 20, 2005, the 2005 Director Compensation Plan was adopted. The shares issued under our 2005 Director Compensation Plan are issued from the 1,000,000 shares reserved for issuance under our Incentive Plan.

Stock Options

At June 30, 2007, 21,000 options were issued and exercisable. During the six months ended June 30, 2007, 2,000 options were exercised and no options were forfeited. These options were excerised through a net exercise transaction, in which 1,473 shares were returned to the Company and 527 shares were issued to the participant.

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There were no options granted during the six months ended June 30, 2007. There were 15,500 options granted and 2,000 options exercised in the six months ended June 30, 2006. No options were forfeited during the six month period ended June 30, 2006.

Nonvested Stock

During the six months ended June 30, 2007, 12,600 nonvested shares of stock were granted to our independent directors under the 2005 Director Compensation Plan. Of these 12,600 shares, 9,100 shares vest in one year, while the remaining 3,500 shares vest one third immediately, and the remaining two-thirds vest over the two year period following the grant date. During the six months ended June 30, 2007, 114,571 nonvested shares were granted to employees pursuant to the 2005 Long-Term Incentive Plan. Of these 114,571 shares, 2,000 shares vest over a three year period while the remaining 112,571 shares vest over a five year period. The fair value of nonvested shares is determined based on the closing trading price of the Company s shares on the grant date. The weighted average grant date fair values of nonvested shares granted during the six month period ended June 30, 2007 were $30.41.

The following table represents the nonvested stock activity for the six months ended June 30, 2007:

	Number of Shares	Weighted average grant date fair value
Nonvested shares outstanding at December 31, 2006	86,716	$ 18.29
Granted	127,171	30.41
Vested	(23,644)	17.64
Forfeited		
Nonvested shares outstanding at June 30, 2007	190,243	$ 26.47

As of June 30, 2007, there was $4.6 million of total unrecognized compensation cost related to nonvested shares granted. That cost is expected to be recognized over the weighted average period of 4.1 years. The total fair value of shares vested in the six month period ended June 30, 2007 was $657,000. During the six months ended June 30, 2006, 8,164 shares vested. The Company records compensation expense related to nonvested share awards at the grant date for shares that are awarded fully vested, and over the vesting term on a straight line basis for shares that vest over time. The Company has recorded $581,000 and $350,000 in compensation expense related to nonvested stock grants in the six months ended June 30, 2007 and 2006 respectively.

Employee Stock Purchase Plan

The Company has a plan whereby eligible employees may purchase the Company s common stock at 95% of the market price on the last day of the calendar quarter. There are 250,000 shares reserved for the plan. The Company issued 3,240 shares of common stock under the plan at a per share price of $27.08 during the three months ended March 31, 2007 and 2,755 shares of common stock under the plan at a per share price of $30.81 during the three months ended June 30, 2007. At June 30, 2007 there were 236,909 shares available for future issuance.

7. Commitments and Contingencies

Contingencies

The terms of several joint venture operating agreements grant a buy/sell option that would require the Company to either purchase or sell the existing membership interest in the joint venture within 30 days of the receipt of the notice to exercise the provision. Either the Company or its joint venture partner has the right to exercise the buy/sell option. The party receiving the exercise notice has the right to either purchase the interests held by the other party or sell its interests to the other party. The purchase price formula for the interests is set forth in the joint venture agreement and is typically based on a multiple of the earnings before income taxes, depreciation and amortization of the joint venture. Total revenue earned by the Company from joint ventures subject to these arrangements was $6.9 million and $7.2 million for the six months ended June 30, 2007 and 2006, respectively. The Company has not received notice from any joint venture partners of their intent to exercise the buy/sell option nor has the Company notified any joint venture partners of any intent to exercise the buy/sell option.

The Company is involved in various legal proceedings arising in the ordinary course of business. Although the results of litigation cannot be predicted with certainty, management believes the outcome of pending litigation will not have a material adverse effect, after considering the effect of the Company s insurance coverage, on the Company s consolidated financial statements.

Compliance

The laws and regulations governing the Company s operations, along with the terms of participation in various government programs, regulate how the Company does business, the services offered, and interactions with patients and the public. These laws and regulations, and their interpretations, are subject to frequent change. Changes in existing laws or regulations, or their interpretations, or the enactment of new laws or regulations could materially and adversely affect the Company s operations and financial condition.

The Company is subject to various routine and non-routine governmental reviews, audits, and investigations. In recent years, federal and state civil and criminal enforcement agencies have heightened and coordinated their oversight efforts related to the healthcare industry, including with respect to referral practices, cost reporting, billing practices, joint ventures, and other financial relationships among healthcare providers. Violation of the laws governing the Company s operations, or changes in the interpretation of those laws, could result in the imposition of fines, civil or criminal penalties, termination of the Company s rights to participate in federal and state-sponsored programs, and suspension or revocation of the Company s licenses.

If the Company s long-term acute care hospitals fail to meet or maintain the standards for Medicare certification as long-term acute care hospitals, such as average minimum length of patient stay, they will receive payments under the prospective payment system applicable to general acute care hospitals rather than payment under the system applicable to long-term acute care hospitals. Payments at rates applicable to general acute care hospitals would likely result in the Company receiving less Medicare reimbursement than currently received for patient services. Moreover, all of the Company s long-term acute care hospitals are subject to additional Medicare criteria because they operate as separate hospitals located in space leased from, and located in, a general acute care hospital, known as a host hospital. This is known as a hospital within a hospital model. These additional criteria include requirements concerning financial and operational separateness from the host hospital.

The Company anticipates there may be changes to the standard episode-of-care payment from Medicare in the future. Due to the uncertainty of the revised payment amount, the Company cannot estimate the impact that changes in the payment rate, if any, will have on its future financial statements.

In August 2004, the Centers for Medicare and Medicaid Services, or CMS, adopted new regulations that implement significant changes affecting long-term acute care hospitals. Among other things, these new regulations, which became effective in October 2004, implemented new rules that provide long-term acute care hospitals operating in the hospital within a hospital model with lower rates of reimbursement for Medicare admissions from their host hospitals that are in excess of specified percentages.

These new rules also reclassified certain long-term acute care hospital diagnosis related groups, which could result in a decrease in reimbursement rates. Further, the new rules kept in place the financial penalties associated with the failure to limit to 5% the total number of Medicare patients discharged to the host hospital and subsequently readmitted to a long-term acute care hospital located within the host hospital.

The Company believes that it is in material compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare program.

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8. Segment Information

The Company s segments consist of (a) home-based services and (b) facility-based services. Home-based services include home nursing services and hospice services. Facility-based services include long-term acute care services and outpatient rehabilitation services. The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

	Three Months Ended June 30, 2007		
	Home-Based Services	Facility-Based Services	Total
		(in thousands)	
Net service revenue	$ 57,992	$ 12,572	$ 70,564
Cost of service revenue	27,711	8,370	36,081
General and administrative expenses	20,797	4,345	25,142
Operating income (loss)	9,484	(143)	9,341
Interest expense	63	31	94
Non-operating income, including gain on sale of assets	213	92	305
Income (loss) from continuing operations before income taxes and minority interest and cooperative endeavor allocations	9,634	(82)	9,552
Minority interest and cooperative endeavor allocations	987	120	1,107
Income (loss) from continuing operations before income taxes	8,647	(202)	8,445
Total assets	$129,856	$ 33,205	$163,061

	Three Months Ended June 30, 2006		
	Home-Based Services	Facility-Based Services	Total
		(in thousands)	
Net service revenue	$36,148	$ 13,820	$ 49,968
Cost of service revenue	16,843	8,255	25,098
General and administrative expenses	12,688	4,045	16,733
Operating income	6,617	1,520	8,137
Interest expense	42	18	60
Non-operating income, including gain on sale of assets	77	39	116
Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations	6,652	1,541	8,193
Minority interest and cooperative endeavor allocations	705	423	1,128
Income from continuing operations before income taxes	5,947	1,118	7,065
Total assets	$84,467	$ 33,328	$117,795

	Six Months Ended June 30, 2007		
	Home-Based Services	Facility-Based Services	Total
		(in thousands)	
Net service revenue	$113,058	$ 26,233	$139,291
Cost of service revenue	53,739	16,959	70,698
General and administrative expenses	38,632	9,178	47,810
Operating income	20,687	96	20,783
Interest expense	116	60	176
Non-operating income, including gain on sale of assets	416	182	598
	20,987	218	21,205

Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations			
Minority interest and cooperative endeavor allocations	2,408	506	2,914
Income (loss) from continuing operations before income taxes	18,579	(288)	18,291
Total assets	$129,856	$ 33,205	$163,061

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	Six Months Ended June 30, 2006		
	Home-Based Services	Facility-Based Services	Total
		(in thousands)	
Net service revenue	$68,569	$ 27,191	$ 95,760
Cost of service revenue	33,097	16,529	49,626
General and administrative expenses	23,988	7,554	31,542
Operating income	11,484	3,108	14,592
Interest expense	95	51	146
Non-operating income, including gain on sale of assets	188	93	281
Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations	11,577	3,150	14,727
Minority interest and cooperative endeavor allocations	1,263	861	2,124
Income from continuing operations before income taxes	10,314	2,289	12,603
Total assets	$84,467	$ 33,328	$117,795

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS

This Management s Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements. Forward-looking statements relate to expectations, beliefs, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts or that necessarily depend upon future events. In some cases, you can identify forward-looking statements by terms such as may, will, should, could, would, expect, plan, intend, anticipate, believe, estimate, project, predict, pote expressions. Specifically, this report contains, among others, forward-looking statements about:

our expectations regarding financial condition or results of operations for periods after June 30, 2007;

our future sources of and needs for liquidity and capital resources;

our expectations regarding any future indebtedness under our credit facility;

our expectations regarding the size and growth of the market for our services;

our business strategies and our ability to grow our business;

the implementation or interpretation of current or future regulations and legislation;

the reimbursement levels of third-party payors;

the effect of adjustments and corrections to prior reimbursement levels by third-party payors on our financial condition or results of operations;

the effect of and applicability of annual caps established by third-party payors on our financial condition or results of operations;

possible changes in legislation and/or government regulations that would affect our business;

possible effects of legal proceedings on our financial condition and results of operations;

the sufficiency of our self-funded medical insurance plan;

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- the impact that the cost of medical supplies may have on our financial condition or results of operations;
- the impact of interest rates on our business;
- our discussion of our disclosure controls and procedures; and
- our discussion of our critical accounting policies.

The forward-looking statements contained in this report reflect our current views about future events, are based on assumptions and are subject to known and unknown risks and uncertainties. Many important factors could cause actual results or achievements to differ materially from any future results or achievements expressed in or implied by our forward-looking statements. Many of the factors that will determine future events or achievements are beyond our ability to control or predict. Important factors that could cause actual results or achievements to differ materially from the results or achievements reflected in our forward-looking statements include, among other things, the factors discussed in the Part II, Item 1A Risk Factors, included in this report and in other of our filings with the SEC, including our annual report on Form 10-K for the year ended December 31, 2006. This report should be read in conjunction with that annual report on Form 10-K, and all our other filings, including quarterly reports on Form 10-Q and current reports on Form 8-K, made with the SEC through the date of this report.

You should read this report, the information incorporated by reference into this report and the documents filed as exhibits to this report completely and with the understanding that our actual future results or achievements may be materially different from what we expect or anticipate.

The forward-looking statements contained in this report reflect our views and assumptions only as of the date this report is signed. Except as required by law, we assume no responsibility for updating any forward-looking statements.

We qualify all of our forward-looking statements by these cautionary statements. In addition, with respect to all of our forward-looking statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Unless the context otherwise requires, we, us, our, and the Company refer to LHC Group, Inc. and its consolidate subsidiaries.

Overview

We provide post-acute healthcare services primarily to Medicare beneficiaries in rural markets in the southern United States. We provide these post-acute healthcare services through our home nursing agencies, hospices, long-term acute care hospitals and outpatient rehabilitation clinic. Since our founders began operations in 1994 with one home nursing agency in Palmetto, Louisiana, we have grown to 155 service providers in Louisiana, Mississippi, Alabama, Texas, Arkansas, West Virginia, Kentucky, Florida, Tennessee, and Georgia as of June 30, 2007. Approximately 58% and 54%, respectively, of our net service revenue for the three months ended June 30, 2007 and 2006 was derived from patients who do not reside in Metropolitan Statistical Areas (MSAs).

Segments

We operate in two segments for financial reporting purposes: home-based services and facility-based services. We derived 82.2% and 72.3% of our net service revenue during the three months ended June 30, 2007 and 2006, respectively, and 81.2% and 71.6% of our net service revenue during the six months ended June 30, 2007 and 2006, respectively, from our home-based services segment and derived the balance of our net service revenue from our facility-based services segment.

Through our home-based services segment we offer a wide range of services, including skilled nursing, private duty nursing, physical, occupational, and speech therapy, medically-oriented social services, and hospice care. As of June 30, 2007, we owned and operated 127 home nursing locations, 8 hospices, a diabetes self management company, a home health pharmacy, and a private duty agency. Of our 138 home-based services locations, 95 are wholly-owned by us and 43 are majority-owned or controlled by us through joint ventures. We also manage the operations of three home nursing agencies in which we have no ownership interest. We intend to increase the number of home nursing agencies that we operate through continued acquisition and development, primarily in underserved rural markets, as we implement our growth strategy. As we acquire and develop home nursing agencies, we anticipate the percentage of our net service revenue and operating income derived from our home-based services segment will increase.

We provide facility-based services principally through our long-term acute care hospitals and outpatient rehabilitation clinic. As of June 30, 2007, we owned and operated four long-term acute care hospitals with seven locations, of which all but one are located within host hospitals. We also owned and operated an outpatient rehabilitation clinic, a pharmacy, two medical equipment locations, a health club, and a critical access hospital. Of these 13 facility-based services locations, seven are wholly-owned by us and six are majority-owned or controlled by us through joint ventures. We also manage the operations of one inpatient rehabilitation facility in which we have no ownership interest. Because of the recent changes in the regulations applicable to long-term acute care hospitals operated as hospitals within hospitals, we do not intend to expand the number of hospital within a hospital long-term acute care hospitals that we operate. Due to our emphasis on expansion through the acquisition and development of home nursing agencies, we anticipate that the percentage of our net service revenue and operating income derived from our facility-based segment will continue to decline.

Recent Developments

Medicare

Home-Based Services. The base payment rate for Medicare home nursing in 2007 is $2,339 per 60-day episode. Since the inception of the prospective payment system in October 2000, the base episode rate payment has varied due to both the impact of annual market basket based increases and Medicare-related legislation. Home health payment rates are updated annually by either the full home health market basket percentage, or by the home health market basket percentage as adjusted by Congress. The Centers for Medicare & Medicaid Services (CMS) establishes the home health market basket index, which measures inflation in the prices of an appropriate mix of goods and services included in home health services.

On June 29, 2007, CMS announced a 3.3% rate increase for hospice care and hospice services provided during the twelve-month period beginning on October 1, 2007 through September 30, 2008. In addition, CMS also announced that the hospice cap amount for the cap year ending October 31, 2007 was $21,410.

On April 27, 2007, CMS issued a Notice of Proposed Rulemaking regarding the Home Health Prospective Payment System Refinement and Rate Update for Calendar Year 2008 (Proposed Rule). The Proposed Rule includes changes to the base rate calculation, refinements to the payment system, and new quality of care data collection requirements, among others. The Proposed Rule was open for public comment for a period of 60 days from the date of the release. On June 22, 2007 we submitted to CMS comments on the Proposed Rule, which comments were filed by us with the SEC on a Form 8-K also dated June 22, 2007. According to the release issued by CMS, the Proposed Rule, including any amendments thereto, will be effective on January 1, 2008. There is no guarantee that the changes and refinements included within the Proposed Rule payment calculations will be included within any final recommendations made by CMS for payments in Calendar year 2008. The Company has decided not to provide speculative net impact reviews to its consolidated financial results of operations and cash flows based upon the Proposed Rule. We will await determination of any final recommendation by CMS for changes to the payment system before determining further reporting needs regarding our Company consolidated financial results.

On April 20, 2007, CMS released a transmittal that provided for a correction of the hospice cap amount for fiscal years ending October 31, 2004 and 2003. As a result of the correction, the new cap amounts are $18,963 and $18,143 for fiscal 2004 and 2003, respectively, compared to the prior rates of $19,636 and $18,661 for fiscal 2004 and 2003, respectively. Management completed an analysis of the Company s potential cap exposure using the corrected rates for both fiscal 2004 and fiscal 2003, and as a result of this analysis, has determined that the change will not have a material impact to the Company s consolidated financial position, cash flows or results of operations.

On April 2, 2007, CMS provided a time extension to health care providers to comply with the National Provider Identifier (NPI) deadline implementation, as required under the regulations of the Health Insurance Portability and Accountability Act (HIPAA) of 1996. The final rule establishes the NPI as the standard unique health provider identifier for health care providers and requires all covered entities to be in compliance with the provisions of such final rule by May 23, 2007 (the NPI Deadline). The NPI is an identifier that is to be used by covered entities to identify health care providers, thus eliminating the current need for multiple identifiers for the same provider. The NPI will be required for use on all health care claims and other HIPAA transactions. The extension has been considered by CMS as it had become apparent that many covered entities were not going to be able to fully comply with the NPI standard by the NPI Deadline. Management has properly assigned the required NPI to each claim that will be processed from the NPI Deadline forward, and management does not foresee the requirement having a material impact to the Company s consolidated financial position, cash flows or results of operations as the Company.

On November 1, 2006, CMS released the final rule updating the home health perspective payment systems for calendar year 2007. The rule finalizes the market basket increase of 3.3%, a 0.2% increase over the proposed rule. This equates to a 3.1% update for urban home health agencies (HHAs) and a 3.6% update for rural HHAs after accounting for changes in the wage index. The update increases the national 60-day episode payment rate for urban home health agencies from the current level of $2,264.38 to $2,339.00. Under the final rule, HHAs will get the full home health market basket as long as they submit required quality data using the Outcome and Assessment Information Set (OASIS). With some limited exceptions, if an HHA does not provide this data, then its home health market basket update of 3.3% will be reduced by two percentage points. The final rule discontinues the temporary 5% add-on payment for rural HHAs in 2007, except for episodes that begin before January 1, 2007. The final rule does not modify the current case-mix methodology for 2007.

In August 2006, CMS announced the payment rates for hospice care furnished from October 1, 2006 through September 30, 2007. These rates are 3.4% higher than the rates for the previous year. In addition, CMS announced that the hospice cap amount for the year ended October 31, 2006 is $20,585.

Facility-Based Services Under the long-term acute care hospital prospective payment system implemented on October 1, 2002, each patient discharged from our long-term acute care hospitals is assigned a long-term care diagnosis-related group (LTACH-DRG). CMS establishes these long-term care diagnosis-related groups by categorizing diseases by diagnosis, reflecting the amount of resources needed to treat a given disease. For each patient, the Company s long-term acute care hospitals are paid a pre-determined fixed amount applicable to the particular LTACH-DRG to which that patient is assigned. The payment is further increased for severity based on co-morbidities, complications, and procedures. The payment is decreased for short-stay outlier patients whose stay does not reach a predetermined minimum assigned for the LTACH-DRG. In addition, extremely high cost patients, after crossing a fixed loss threshold, receive an additional high-cost outlier payment intended to account for resource utilization requirements above the LTACH-DRG payment.

On May 2, 2007 CMS published its annual long-term acute care hospital update for the LTACH Rate Year which begins July 1, 2007. There are five major portions of the final rule that are noteworthy for the operations of our long-term acute care hospitals. The Final Rule projects an overall decrease in payments to all Medicare certified long-term acute care hospitals of 3.8% compared to an impact estimated at 2.9% under the proposed rule. Included in the Final Rule are the following: (1) an increase to the standard federal payment rate of 0.71% which is a base rate of $38,356.45; (2) revisions to payment methodologies impacting short stay outliers, which reduce payments by 0.9%; (3) adjustments to the wage index component of the federal payment resulting in projected reductions in payments of 1.0%; (4) an increase in the high cost outlier threshold from $18,477 per discharge in the proposed rule to $22,954 in the Final Rule resulting in projected reductions of 2.5%; and (5) an extension of the policy known as the 25 Percent Rule to all LTAC hospitals, with a three-year phase-in, which CMS projects will not result in payment reductions for the first year of implementation but estimates reductions of 2.4% in the second year of implementation. The Final Rule also states that the annual update to the LTACH-DRG classifications and relative

weights will be made in a budget neutral manner; effective October 1, 2007, which means that even after annual re-weighting of LTACH-DRGs, total payments to LTACHs will not be reduced in 2008.

Our analysis has shown that the impact of this final rule to be a 3.29% reduction in payments to the Company s long-term acute care hospitals. This reduction is less than the projected decrease of 3.8% forecast by CMS in the final rule. The Company currently operates a total of seven long-term acute care hospitals. Six of our hospitals are classified as hospitals within a hospital (HwH) and one is classified as a freestanding.

The final rule regarding extension of the 25 Percent Rule to freestanding facilities will not have an effect on our one existing freestanding location based on our analysis that no single referral source is greater than 25% of Medicare discharges.

Under Medicare, we are reimbursed for rehabilitation services based on a fee schedule for services provided adjusted by the geographical area in which the facility is located. Outpatient therapy services are subject to an annual cap of $1,780 per beneficiary effective January 1, 2007. The Deficit Reduction Act of 2005 and the Tax Relief and Health Care Act of 2006 provided for an exceptions process that effectively prevents application of the caps. The exceptions process ends January 1, 2008. We are unable to predict whether Congress will extend the exceptions process for 2008. We cannot assure you that one or more of our outpatient rehabilitation clinics will not exceed the caps in the future.

Office of Inspector General

The Office of Inspector General (OIG) has a responsibility to report both to the Secretary of the Department of Health and Human Services and to Congress any program and management problems related to programs such as Medicare. The OIG s duties are carried out through a nationwide network of audits, investigations and inspections. Each year, the OIG outlines areas it intends to study relating to a wide range of providers. In fiscal year 2007, the OIG indicated its intent to study topics relating to, among others, home health, hospice, long-term care hospitals, and certain outpatient rehabilitation services. No estimate can be made at this time regarding the impact, if any, of the OIG s findings.

Components of Expenses

Cost of Service Revenue

Our cost of service revenue consists primarily of the following expenses incurred by our clinical and clerical personnel in our agencies and facilities:

- salaries and related benefits;
- transportation, primarily mileage reimbursement; and
- supplies and services, including payments to contract therapists.

General and Administrative Expenses

Our general and administrative expenses consist primarily of the following expenses incurred by our home office and administrative field personnel:

Home office:

- salaries and related benefits;
- insurance;
- costs associated with advertising and other marketing activities; and
- rent and utilities;

Supplies and services:
- accounting, legal and other professional services; and
- office supplies;

Depreciation; and

Provision for bad debts.

Results of Operations

Three Months Ended June 30, 2007 Compared to Three Months Ended June 30, 2006

Net Service Revenue

Net service revenue for the three months ended June 30, 2007 was $70.6 million, an increase of $20.6 million, or 41.2%, from $50.0 million in 2006. The increase in net service revenue is due primarily to the increase in patient census in the home-based segment through acquisitions and internal growth. For the three months ended June 30, 2007 and 2006, 82.0% and 85.8% respectively, of our net service revenue was derived from Medicare.

Home-Based Services.

Net home-based services revenue for the three months ended June 30, 2007 was $58.0 million, an increase of 60.4%, from $36.1 million for the three months ended June 30, 2006. Organic growth in this service sector was approximately $16.5 million, or 54.4%. The increase in net home-based service revenue is due primarily to the increase in patient census through acquisitions and internal growth. Total admissions were 10,277 during the period, versus 5,852 for the same period in 2006, a 75.6% increase. Organic growth in admissions was 70.7%. The Company also monitors patient census as a key performance indicator within its home-based services. Average home-based patient census for the three months ended June 30, 2007 was 16,283 patients, an increase of 66.0% as compared to 9,807 patients for the three months ended June 30, 2006. Organic growth in home-based patient census was 59.8%. Organic growth includes growth on same store locations (owned for greater than 12 months), and growth from de novo locations. Growth from acquired locations owned less than 13 months is not included.

	For the three months ended June 30,			For the three months ended June 30,			For the three months ended June 30,		
	2007 Revenue	2006 Revenue	% Growth	2007 Admissions	2006 Admissions	% Growth	2007 Census	2006 Census	% Growth
Organic	$46,756	$30,280	54.4%	7,362	4,312	70.7%	12,779	7,996	59.8%
Acquired	$11,236	$ 5,868	91.5%	2,915	1,540	89.3%	3,504	1,811	93.5%
Total	$57,992	$36,148	60.4%	10,277	5,852	75.6%	16,283	9,807	66.0%

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	For the three months ended June 30,			For the three months ended June 30,			For the three months ended June 30,		
	2007 Medicare Census	2006 Medicare Census	% Growth	2007 Medicare Admits	2006 Medicare Admits	% Growth	2007 Medicare Episodes	2006 Medicare Episodes	% Growth
Organic	10,170	6,635	53.3%	5,278	3,227	63.6%	16,258	10,725	51.6%
Acquired	2,052	1,309	56.8%	1,831	983	86.3%	3,002	1,252	139.8%
Total	12,222	7,944	53.9%	7,109	4,210	68.9%	19,260	11,977	60.8%

Facility-Based Services.

Net service revenue for facility-based services for the three months ended June 30, 2007, decreased 9.0% to $12.6 million compared with $13.8 million for the three months ended June 30, 2006. The decrease in facility-based net service revenue is due primarily to the revenue adjustment of $1.1 million taken in the second quarter relating to commercial patients in the Long-Term Acute Care Hospitals (LTACHs). For additional information on the revenue and bad debt adjustments in the LTACHS, see Item 1, Financial Statements Notes to the Unaudited Consolidated Financial Statements Note 1 Adjustment to Net Service Revenue and Bad Debt Expense. Patient days increased 3.1% to 11,453 in the three months ended June 30, 2007, from 11,110 in the three months ended June 30, 2006.

	For the three months ended June 30,			For the three months ended June 30,			For the three months ended June 30,		
	2007 Revenue	2006 Revenue	% Growth	2007 Patient Days	2006 Patient Days	% Growth	2007 Discharges	2006 Discharges	% Growth
Organic	$12,572	$13,820	(9.0)%	11,453	11,110	3.1%	451	430	4.9%
Acquired			%			%			%
Total	$12,572	$13,820	(9.0)%	11,453	11,110	3.1%	451	430	4.9%

Cost of Service Revenue

Cost of service revenue for the three months ended June 30, 2007 was $36.1 million, an increase of $11.0 million, or 43.8%, from $25.1 million for the three months ended June 30, 2006. Cost of service revenue represented approximately 51.1% and 50.2% of our net service revenue for the three months ended June 30, 2007 and 2006, respectively.

Home-Based Services. Cost of home-based services revenue for the three months ended June 30, 2007 was $27.7 million, an increase of $10.9 million, or 64.5%, from $16.8 million for the three months ended June 30, 2006. Approximately $9.1 million of this increase resulted from an increase in salaries and benefits. Approximately $6.8 million of the increase in salaries and benefits expense was due to acquisitions that occurred in 2006 and approximately $2.1 million of the increase in salaries and benefits expense was due to acquisitions that occurred in 2007. The remaining increase in salaries and benefits expense of approximately $127,000 was primarily attributable to internal growth. The remaining increase in cost of service revenue was attributable to increases in supplies and services expense and transportation expense. Supplies and service expense increased approximately $674,000. Of this $674,000, approximately $517,000 of the increase in supplies and services expense was due to acquisitions in 2006 while $157,000 was due to acquisitions in 2007. Transportation expense increased approximately $1.1 million. Of this

$1.1 million, approximately $672,000 of the increase in transportation expense was due to acquisitions in 2006, $217,000 was due to acquisitions in 2007, and $234,000 was due to internal growth. Cost of home-based services revenue represented approximately 47.8% and 46.6% of our net home-based services revenue for the three months ended June 30, 2007 and 2006, respectively.

Facility-Based Services. Cost of facility-based services revenue for the three months ended June 30, 2007 was $8.4 million, an increase of $100,000 or 1.4%, from $8.3 million for the three months ended June 30, 2006. The entire increase resulted from an increase in supplies from internal growth. The increase in supplies is due to the increase in patient days. Cost of facility-based service revenue represented approximately 66.5% and 59.7% of our net facility-based services revenue for the three months ended June 30, 2007 and 2006, respectively.

General and Administrative Expenses

General and administrative expenses for the three months ended June 30, 2007 were $25.1 million, an increase of $8.4 million, or 50.3%, from $16.7 million for the three months ended June 30, 2006. General and administrative expenses represented approximately 35.6% and 33.5% of our net service revenue for the three months ended June 30, 2007 and 2006, respectively.

Home-Based Services. General and administrative expenses in the home-based services segment for the three months ended June 30, 2007 were $20.8 million, an increase of $8.1 million, or 63.9%, from $12.7 million for the three months ended June 30, 2006. Approximately $4.3 million of the increase in general and administrative expenses was due to acquisitions that occurred in 2006 and approximately $1.8 million of the increase in general and administrative expenses were due to acquisitions that occurred in 2007. The remaining increase in general and administrative expenses of approximately $2.0 million was primarily attributable to internal growth. Of the $2.0 million attributable to internal growth, $805,000 is related to an increase in bad debt expense. General and administrative expenses in the home-based services segment represented approximately 35.9% and 35.1% of our net service revenue for the three months ended June 30, 2007 and 2006, respectively.

Facility-Based Services. General and administrative expenses for the three months ended June 30, 2007 were $4.3 million, an increase of $300,000, or 7.4%, from $4.0 million for the same period in 2006. The entire growth was attributable to internal growth and is due to an increase in bad debt expense. General and administrative expenses in the facility-based services segment represented approximately 34.6% and 29.3% of our net service revenue for the three months ended June 30, 2007 and 2006, respectively.

Income Tax Expense

The effective tax rates for the three months ended June 30, 2007 and 2006 were 36.4% and 36.5% respectively.

Minority Interest and Cooperative Endeavor Allocations

The minority interest and cooperative endeavor allocations expense remained consistent for the three months ended June 30, 2007 at $1.1 million, compared to $1.1 million for the same period in 2006.

Discontinued Operations

Revenue from discontinued operations for the three months ended June 30, 2007 and 2006 was $1.0 million and $1.3 million, respectively. Costs, expenses, and minority interest and cooperative endeavor allocations were $1.6 million and $1.7 million, respectively, for the three months ended June 30, 2007 and 2006. For the three months ended June 30, 2007, the loss from discontinued operations was $336,000 as compared to a loss from discontinued operations of $271,000 for the same period in 2006. In the second quarter of 2007, the Company placed its critical access hospital into discontinued operations.

Six Months Ended June 30, 2007 Compared to Six Months Ended June 30, 2006

Net Service Revenue

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Net service revenue for the six months ended June 30, 2007 was $139.3 million, an increase of $43.5 million, or 45.5%, from $95.8 million in 2006. The increase in net service revenue is due primarily to the increase in patient census in the home-based segment through acquisitions and internal growth. For the six months ended June 30, 2007 and 2006, 82.0% and 86.1% respectively, of our net service revenue was derived from Medicare.

Home-Based Services.

Net home-based services revenue for the six months ended June 30, 2007 was $113.1 million, an increase of 64.9%, from $68.6 million for the six months ended June 30, 2006. Organic growth in this service sector was approximately $32.0 million, or 53.1%. The increase in net home-based service revenue is due primarily to the increase in patient census through acquisitions and internal growth. Total admissions were 20,442 during the period, versus 11,422 for the same period in 2006, a 79.0% increase. Organic growth in admissions was 72.8%. Average home-based patient census for the six months ended June 30, 2007 was 16,009 patients, an increase of 67.9% as compared to 9,535 patients for the six months ended June 30, 2006. Organic growth in home-based patient census was 62.0%.

	For the six months ended June 30,			**For the six months ended June 30,**			**For the six months ended June 30,**		
	2007 Revenue	2006 Revenue	% Growth	2007 Admissions	2006 Admissions	% Growth	2007 Census	2006 Census	% Growth
Organic	$ 92,422	$60,379	53.1%	14,969	8,665	72.8%	12,608	7,785	62.0%
Acquired	$ 20,636	$ 8,190	152.0%	5,473	2,757	98.5%	3,401	1,750	94.3%
Total	$113,058	$68,569	64.9%	20,442	11,422	79.0%	16,009	9,535	67.9%

	For the six months ended June 30,			**For the six months ended June 30,**			**For the six months ended June 30,**		
	2007 Medicare Census	2006 Medicare Census	% Growth	2007 Medicare Admits	2006 Medicare Admits	% Growth	2007 Medicare Episodes	2006 Medicare Episodes	% Growth
Organic	9,925	6,439	54.1%	10,736	6,428	67.0%	31,550	20,971	50.4%
Acquired	2,069	1,208	71.3%	3,351	1,860	80.2%	4,874	2,040	138.9%
Total	11,994	7,647	56.8%	14,087	8,288	70.0%	36,424	23,011	58.3%

Facility-Based Services.

Net service revenue for facility-based services for the six months ended June 30, 2007, decreased 3.5% to $26.2 million compared with $27.2 million for the six months ended June 30, 2006. The decrease in facility-based net service revenue is due primarily to the revenue adjustment of $1.1 million taken in the six months ended June 30, 2007, relating to commercial patients in the LTACHs. For additional information on the revenue and bad debt adjustments in the LTACHS, see Item 1, Financial Statements Notes to the Unaudited Consolidated Financial Statements Note 1 Adjustment to Net Service Revenue and Bad Debt Expense. Patient days increased 4.5% to 23,127 in the six months ended June 30, 2007, from 22,140 in the three months ended June 30, 2006.

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	For the six months ended June 30,			For the six months ended June 30,			For the six months ended June 30,		
	2007 Revenue	2006 Revenue	% Growth	2007 Patient Days	2006 Patient Days	% Growth	2007 Discharges	2006 Discharges	% Growth
Organic	$26,233	$27,191	(3.5)%	23,127	22,140	4.5%	922	883	4.4%
Acquired			%			%			%
Total	$26,233	$27,191	(3.5)%	23,127	22,140	4.5%	922	883	4.4%

Cost of Service Revenue

Cost of service revenue for the six months ended June 30, 2007 was $70.7 million, an increase of $21.1 million, or 42.5%, from $49.6 million for the six months ended June 30, 2006. Cost of service revenue represented approximately 50.8% and 51.8% of our net service revenue for the six months ended June 30, 2007 and 2006, respectively.

Home-Based Services. Cost of home-based services revenue for the six months ended June 30, 2007 was $53.7 million, an increase of $20.6 million, or 62.4%, from $33.1 million for the six months ended June 30, 2006. Approximately $17.7 million of this increase resulted from an increase in salaries and benefits. Approximately $13.4 million of the increase in salaries and benefits expense was due to acquisitions that occurred in 2006 and approximately $3.3 million of the increase in salaries and benefits expense was due to acquisitions that occurred in 2007. The remaining increase in salaries and benefits expense of approximately $1.0 million was primarily attributable to internal growth. The remaining increase in cost of service revenue was attributable to increases in supplies and services expense and transportation expense. Supplies and service expense increased approximately $1.2 million. Of this $1.2 million, approximately $1.0 million of the increase in supplies and services expense was due to acquisitions in 2006 while $139,000 was due to acquisitions in 2007. Transportation expense increased approximately $1.7 million. Of this $1.7 million, approximately $1.2 million of the increase in transportation expense was due to acquisitions in 2006, $308,000 was due to acquisitions in 2007, and $214,000 was due to internal growth. Cost of home-based services revenue represented approximately 47.5% and 48.3% of our net home-based services revenue for the six months ended June 30, 2007 and 2006, respectively.

Facility-Based Services. Cost of facility-based services revenue for the six months ended June 30, 2007 was $17.0 million, an increase of $430,000 or 2.6%, from $16.5 million for the six months ended June 30, 2006. The entire increase resulted from an increase in supplies from internal growth. The increase in supplies is due to the increase in patient days. Cost of facility-based service revenue represented approximately 64.6% and 60.8% of our net facility-based services revenue for the six months ended June 30, 2007 and 2006, respectively.

General and Administrative Expenses

General and administrative expenses for the six months ended June 30, 2007 were $47.8 million, an increase of $16.3 million, or 51.6%, from $31.5 million for the six months ended June 30, 2006. General and administrative expenses represented approximately 34.3% and 32.9% of our net service revenue for the six months ended June 30, 2007 and 2006, respectively.

Home-Based Services. General and administrative expenses in the home-based services segment for the six months ended June 30, 2007 were $38.6 million, an increase of $14.6 million, or 61.0%, from $24.0 million for the six months ended June 30, 2006. Approximately $4.0 million of the increase in general and administrative expenses was due to acquisitions that occurred in 2006 and approximately $2.4 million of the increase in general and administrative expenses were due to acquisitions that occurred in 2007. The remaining increase in general and administrative expenses of approximately $8.2 million was primarily attributable to internal growth. Of the $8.2 million attributable to internal growth, $1.4 million is related to an increase in bad debt expense. General and administrative expenses in the home-based services segment represented approximately 34.2% and 35.0% of our net service revenue for the six months ended June 30, 2007 and 2006, respectively.

Facility-Based Services. General and administrative expenses for the six months ended June 30, 2007 were $9.2 million, an increase of $1.6 million, or 21.5%, from $7.6 million for the same period in 2006. The entire growth was attributable to internal growth. Of the $1.6 million attributable to internal growth, $715,000 is due to an increase in bad debt expense. General and administrative expenses in the facility-based services segment represented approximately 35.0% and 27.8% of our net service revenue for the six months ended June 30, 2007 and 2006, respectively.

Income Tax Expense

The effective tax rates for the six months ended June 30, 2007 and 2006 were 37.6% and 34.2% respectively. The effective tax rate increase in the six months ended June 30, 2007 is primarily due to the reduction in the tax credits related to the Gulf Opportunity Zone Act of 2005.

Minority Interest and Cooperative Endeavor Allocations

The minority interest and cooperative endeavor allocations expense for the six months ended June 30, 2007 was $2.9 million, compared to $2.1 million for the same period in 2006. The increase is due primarily to an increase in joint ventures and an increase in the income from operations related to our joint ventures.

Discontinued Operations

Revenue from discontinued operations for the six months ended June 30, 2007 and 2006 was $2.1 million and $3.5 million, respectively. Costs, expenses, and minority interest and cooperative endeavor allocations were $3.0 million and $4.4 million, respectively, for the six months ended June 30, 2007 and 2006. For the six months ended June 30, 2007, the loss from discontinued operations was $597,000, as compared to a loss from discontinued operations of $536,000 for the same period in 2006. In the first quarter of 2007, the Company converted Louisiana Extended Care Hospital of West Monroe back into continuing operations from discontinued operations. After having the entity in discontinued operations for the year ended December 31, 2006, the Company decided to make this change after we did not receive an offer that we felt was indicative of the value of the entity. In the first quarter of 2007, the Company placed one pharmacy location into discontinued operations, and in the second quarter of 2007, the Company placed its critical access hospital into discontinued operations.

Liquidity and Capital Resources

Our principal source of liquidity for our operating activities is the collection of our accounts receivable, most of which are collected from governmental and third party commercial payors. Our reported cash flows from operating activities are impacted by various external and internal factors, including the following:

Operating Results Our net income has a significant impact on our operating cash flows. Any significant increase or decrease in our net income could have a material impact on our operating cash flows.

Start-Up Costs Following the completion of an acquisition, we generally incur substantial start-up costs in order to implement our business strategy. There is generally a delay between our expenditure of these start-up costs and the increase in net service revenue, and subsequent cash collections, which adversely affects our cash flows from operating activities.

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Timing of Payroll Our employees are paid bi-weekly on Fridays; therefore, operating cash flows decline in reporting periods that end on a Friday. Conversely, for those reporting periods ending on a day other than Friday, our cash flows are higher because we have not yet paid our payroll.

Medical Insurance Plan Funding We are self funded for medical insurance purposes. Any significant changes in the amount of insurance claims submitted could have a direct impact on our operating cash flows.

Medical Supplies A significant expense associated with our business is the cost of medical supplies. Any increase in the cost of medical supplies, or in the use of medical supplies by our patients, could have a material impact on our operating cash flows.

Operating activities during the six months ended June 30, 2007 provided $471,000 in cash compared to $12.1 million for the six months ended June 30, 2006. Net income provided cash of $10.8 million. Non-cash items such as depreciation and amortization, provision for bad debts, equity-based compensation, minority interest in earnings of subsidiaries and deferred income taxes totaled $8.5 million. These non-cash charges are offset primarily by an increase in accounts receivable of $13.8 million due to increased revenue and an increase in prepaid federal and state income taxes of $3.4 million.

Days sales outstanding, or DSO, for the three months ended June 30, 2007, was 75 days as compared with 74 days for the same three-month period in 2006. DSO, when adjusted for acquisitions and unbilled accounts receivables, was 70 days. The adjustment takes into account $3.7 million of unbilled receivables that the Company is delayed in billing due to the lag time in receiving the change of ownership after acquiring companies. For the comparable period in 2006, adjusted DSO was 65 days, taking into account $4.6 million in unbilled accounts receivable.

Investing activities used $11.0 million and $6.8 million in cash for the six months ended June 30, 2007 and 2006, respectively. In the six months ended June 30, 2007, cash used by investing activities was $1.5 million for the purchases of property and equipment consisting primarily of computer hardware, software, and licenses, and $9.5 million in the cost of acquisitions.

Financing activities used $3.0 million and $3.6 million in the six months ended June 30, 2007 and 2006, respectively. The $3.0 million cash used in financing activities in the six months ended June 30, 2007 was for minority interest distributions.

At June 30, 2007, we had working capital of $69.4 million compared to $68.4 million at December 31, 2006, an increase of $1.0 million. This increase in working capital was due primarily to increases in accounts receivable due to increased revenue.

Indebtedness

Our total long-term indebtedness was $3.6 million at June 30, 2007 and $3.8 million at December 31, 2006, respectively, including the current portions of $558,000 and $639,000. In April 2005, we entered into an amended and restated senior secured credit facility with Residential Funding Corporation due April 15, 2010. We, together with certain of our subsidiaries, may become borrowers under the credit facility. Our obligations and the obligations of our subsidiary borrowers under our credit facility agreement are secured by a lien on substantially all of our assets (including the capital stock or other forms of ownership interests we hold in our subsidiaries and affiliates) and the assets of those subsidiaries and affiliates.

Our credit facility makes available to us up to $22.5 million in revolving loans. The total availability may be increased up to a maximum of $25.0 million, subject to certain terms and conditions. Total availability under our credit facility may be limited from time to time based on the value of our receivables. As of June 30, 2007, we had no outstanding balance under our credit facility.

Interest on outstanding borrowings under our credit facility accrues at a variable base rate (based on Wells Fargo Bank s prime rate or the federal funds rate), plus a margin of 1.5%.

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Our credit facility contains customary affirmative, negative and financial covenants. For example, we are restricted in incurring additional debt, disposing of assets, making investments, allowing fundamental changes to our business or organization, and making certain payments in respect of stock or other ownership interests, such as dividends and stock repurchases. Financial covenants include requirements that we maintain a debt to EBITDA ratio of no greater than 1.5 to 1.0 and a fixed-charge coverage ratio of not less than 1.4 to 1.0.

Our credit facility also contains customary events of default. These include bankruptcy and other insolvency events, cross-defaults to other debt agreements, a change in control involving us or any subsidiary guarantor, and the failure to comply with certain covenants.

Contingencies

For a discussion of contingencies, see Item 1, Notes to Consolidated Financial Statements Note 7 Commitments and Contingencies of this Form 10-Q, which discussion is incorporated herein by reference.

Off-Balance Sheet Arrangements

We do not currently have any off-balance sheet arrangements with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. In addition, we do not engage in trading activities involving non-exchange traded contracts. As such, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in these relationships.

Critical Accounting Policies

For a discussion of critical accounting policies, see Item 1, Notes to Consolidated Financial Statements Note 2 Significant Accounting Policies of this Form 10-Q, which discussion is incorporated herein by reference.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of June 30, 2007, we had cash of $13.3 million, which consisted of highly liquid money market instruments with maturities less than 90 days. Because of the short maturities of these instruments, a sudden change in market interest rates would not be expected to have a material impact on the fair value of the portfolio. We would not expect our operating results or cash flows to be materially affected by the effect of a sudden change in market interest rates on our portfolio. At times, cash in banks is in excess of the FDIC insurance limit. The Company has not experienced any loss as a result of those deposits and does not expect any in the future.

Our exposure to market risk relates to changes in interest rates for borrowings under the senior secured credit facility we entered into in April 2005. A hypothetical 100 basis point adverse move (increase) in interest rates would not have materially affected the interest expense for the six months ended June 30, 2007 since there were no amounts outstanding on the credit agreement during this period.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)) that are designed to ensure that information required to be disclosed in the Company s reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms. Such information is also accumulated and communicated to management, including the Company s Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Management of the Company, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company s disclosure controls and procedures and based on that evaluation, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company had a material weakness related to the controls over the recording of contractual adjustments on commercial contract claims in its Long-Term Acute Care Hospital (LTACH) business. The Company s management, including the Company s principal executive and principal financial officers, has concluded that the Company s disclosure controls and procedures were not effective as of June 30, 2007. To address the material weakness described above, the Company has implemented additional manual controls and procedures over the recording of contractual adjustments related to commercial contracts in the LTACHs. The Company will work with outside consultants to continue identifying the appropriate methods of ensuring these controls and procedures may not be circumvented in the future.

The design of any system of control is based upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated objectives under all future events, no matter how remote, or that the degree of compliance with the policies or procedures may not deteriorate. Because of their inherent limitations, disclosure controls and procedures may not prevent or detect all misstatements. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

Changes in Internal Controls

Other than the matter described in this Item 4, there have been no changes in the Company s internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) that occurred during the three months ended June 30, 2007, that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

We are involved in litigation and proceedings in the ordinary course of business. We do not believe that the outcome of any of the matters in which we are currently involved, individually or in the aggregate, will have a material adverse effect upon our business, financial condition, or results of operations.

ITEM 1A. RISK FACTORS.

There have been no material changes from the Risk Factors we previously disclosed in our Form 10-K for the year ended December 31, 2006 filed with the Securities and Exchange Commission on March 16, 2007.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

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ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Our annual meeting of stockholders was held on June 14, 2007. At the annual meeting, the following matters were voted on with the following results:

Election of Directors. At the annual meeting, John L. Indest, Ronald T. Nixon, and W.J. Billy Tauzin were elected to serve as Class II directors for three-year terms expiring at the 2010 annual meeting of stockholders. Voting results were as follows:

Name of Director	Votes For	Votes Withheld
John L. Indest	16,904,047	121,723
Ronald T. Nixon	16,903,983	121,787
W.J. Billy Tauzin	16,900,280	125,490

The following persons continued as directors following the annual meeting: Keith G. Myers, Ted W. Hoyt, George A. Lewis, Nancy G. Brinker, John B. Breaux, and Dan S. Wilford.

Ratification of Appointment of Independent Auditors. At the annual meeting, the stockholders approved the appointment of the independent accounting firm of Ernst & Young LLP to serve as the Company s independent auditors. Voting results were as follows:

Votes For	Votes Withheld	Abstentions
16,749,487	263,569	12,714

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS.

3.1	Certificate of Incorporation of LHC Group, Inc. (previously filed as an exhibit to the Form S-1/A (File No. 333-120792) on February 14, 2005).
3.2	Bylaws of LHC Group, Inc. (previously filed as an exhibit to the Form S-1/A (File No. 333-120792) on May 9, 2005).
4.1	Specimen Stock Certificate of LHC s Common Stock, par value $0.01 per share (previously filed as an exhibit to the Form S-1/ A (File No. 333-120792) on February 14, 2005).
4.2	Reference is made to Exhibits 3.1 and 3.2 (previously filed as an exhibit to the Form S-1/A (File No. 333-120792) on February 14, 2005 and May 9, 2005, respectively).
31.1	Certification of Keith G. Myers, Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Barry E. Stewart, Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32*	Certification of Chief Executive Officer and Chief Financial Officer of LHC Group, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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* This exhibit is furnished to the SEC as an accompanying document and is not deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that Section, and the document will not be deemed incorporated by reference into any filing under the Securities Act of 1933.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	LHC GROUP, INC.
Date August 9, 2007	/s/ Barry E. Stewart Barry E. Stewart Executive Vice President and Chief Financial Officer

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