

THOMSON REUTERS STREETEVENETS

EDITED TRANSCRIPT

ANTM - Q1 2018 Anthem Inc Earnings Call

EVENT DATE/TIME: APRIL 25, 2018 / 12:30PM GMT



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

CORPORATE PARTICIPANTS

Brian Thomas Griffin *Anthem, Inc. - Executive VP & CEO of IngenioRX*

Chris Rigg *Anthem, Inc. - VP, Investor Relations*

Gail Koziara Boudreaux *Anthem, Inc. - President, CEO & Director*

John Edward Gallina *Anthem, Inc. - Executive VP & CFO*

Peter David Haytaian *AMERIGROUP Corporation - Former CEO of Northeastern Region, CEO & President of Amerigroup New Jersey Inc*

CONFERENCE CALL PARTICIPANTS

Albert J. William Rice *Crédit Suisse AG, Research Division - Research Analyst*

Anagha A. Gupte *Leerink Partners LLC, Research Division - MD, Healthcare Services and Senior Research Analyst*

David Howard Windley *Jefferies LLC, Research Division - Equity Analyst*

Gary Paul Taylor *JP Morgan Chase & Co, Research Division - Analyst*

Joshua Richard Raskin *Nephron Research LLC - Research Analyst*

Justin Lake *Wolfe Research, LLC - MD & Senior Healthcare Services Analyst*

Kevin Mark Fischbeck *BofA Merrill Lynch, Research Division - MD in Equity Research*

Peter Heinz Costa *Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

Ralph Giacobbe *Citigroup Inc, Research Division - Director*

Stephen Vartan Tanal *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Zachary William Sopcak *Morgan Stanley, Research Division - VP on the Healthcare Services and Distribution Team*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. And welcome to the Anthem first quarter results conference call. (Operator Instructions)

As a reminder, this conference is being recorded. And I would now like to turn the conference over to the company's management.

Chris Rigg - *Anthem, Inc. - VP, Investor Relations*

Good morning, and welcome to Anthem's First Quarter 2018 Earnings Call. This is Chris Rigg, Vice President of Investor Relations. And with us this morning are Gail Boudreaux, President and CEO; John Gallina, our CFO; Peter Haytaian, President of our Commercial & Specialty Business Division; Brian Griffin, CEO of IngenioRx; Dr. Tunde Sotunde, President Medicaid; Marc Russo, President Medicare; and Tom Zielinski, our General Counsel.

Gail will begin the call by giving an overview of our first quarter financial results, followed by commentary around our focus on execution, leadership rotations and growth priorities. John will then discuss our key financial metrics in greater detail and go over our updated 2018 outlook. We will then be available for Q&A.

During the call, we will reference certain non-GAAP measures. Reconciliations of these non-GAAP measures to the most directly comparable GAAP measures are available on our website at antheminc.com.



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

We will also be making some forward-looking statements on this call. Listeners are cautioned that these statements are subject to certain risks and uncertainties, many of which are difficult to predict and generally beyond the control of Anthem. These risks and uncertainties can cause actual results to differ materially from our current expectations. We advise the listeners to carefully review the risk factors discussed in today's press release and in our quarterly filings with the SEC.

I will now turn the call over to Gail.

Gail Koziara Boudreaux - Anthem, Inc. - President, CEO & Director

Good morning, everyone. Thank you for joining us for Anthem's First Quarter 2018 Earnings Call. This morning, we reported first quarter 2018 GAAP earnings per share of \$4.99 and adjusted earnings per share of \$5.41, which were ahead of expectations, driven by strong medical cost performance and improved operating margins.

During the quarter, we completed the acquisition of America's 1st Choice, which added 135,000 Medicare Advantage lives in Central Florida. This acquisition, along with the acquisition of HealthSun in late 2017, aligns with our strategy to grow our business through deep integration in the markets we serve. Anthem is now the third largest Medicare Advantage plan in the fast-growing Florida market, serving more than 225,000 members in the central and southern portions of the state. With the addition of America's 1st Choice and HealthSun, Anthem is now the only national health care company to offer 5 5-star Medicare Advantage plans.

First quarter operating revenues were relatively flat at \$22.3 billion, due primarily to a reduction in individual membership resulting from planned exits in the ACA-compliant marketplace. Revenues for Government Business grew 10% year-over-year as a result of our continued focus on quality and our leadership in serving the complex social and medical requirements of the dual special needs population.

Growth in service fee revenue reflects increased sales of our member and clinical engagement programs to self-funded customers, an area where we see additional growth opportunity. Anthem's medical cost ratio came in at a better-than-expected 81.5%. The better-than-expected results reflect our commitment to strong medical cost performance by effectively leveraging community-based, innovative and integrated clinical and value-based care arrangements across our markets.

Our SG&A ratio was in line with expectations at 15.3%, leading to a favorable first quarter operating margin of 8.4%. Based on our strong first quarter financial performance, the strengthening of our operating discipline and our updated expectations for the remainder of the year, we are raising our full year 2018 adjusted earnings per share outlook to greater than \$15.30, a 27% increase from 2017. We are intensely focused on delivering on our financial commitments, optimizing execution across our business segments, offering even greater value for those we serve and investing wisely in our future growth.

During the quarter, we continued to make strategic investments in technology modernization, population and consumer digital health, data analytics and product development capabilities to enhance our consumer experience, increase speed to market and position Anthem to respond to the evolving needs of our customers and the changing health care environment.

Moving beyond financial performance, we continue to align our organization and investments to accelerate growth across Anthem and more effectively leverage our strong brand and local market position. We expect continued growth across our Government Business and our fee-based Commercial membership throughout the remainder of the year. The solid growth in our fee-based membership during the quarter reflects our focus on combining Anthem's best-in-class medical position with innovative consumer engagement programs, flexible network strategies and integrated clinical management tool.

Anthem Health Guide is an example of one of those programs. Health Guide helps employers manage their total cost of care through improved consumer engagement and an integrated clinical and customer service model, and to date, more than 5 million individuals are enrolled in the program. For every dollar invested in Health Guide, employers realize up to \$4 in saving. Anthem Engage is another example of how we're improving the consumer experience through digital capabilities that provide real time access to information and a range of personalized tools to help our

APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

members make better health decisions. Roughly 800,000 Anthem members have already adopted Anthem Engage after its launch this quarter, and we expect that number to more than double over the next 12 months.

We're disappointed in the decline of our large group insured membership where the reintroduction of the insurer fee negatively impacted persistency and a greater-than-expected number of customers converted from insured to self-funded. We recognize that we did not respond quickly enough to market dynamics and competitor actions with more affordable product options to help offset the impact of the insurer fee.

Going forward, the investments we're making in modularization and product development along with better alignment of our segment and local market leadership will enable us to more effectively leverage information and respond to changes across all of our markets while maintaining our disciplined approach to pricing.

Our newly established sales effectiveness organization is focused on driving Commercial sales through an increasingly sophisticated, coordinated go-to-market strategy that we expect to translate into membership growth for the remainder of 2018 and into 2019.

In Medicaid, we continue to develop strategic partnerships with other health plans and care provider that combine our best-in-class Medicaid operating platform with their local market expertise. During the quarter, we launched a new Medicaid joint venture with the Arkansas Provider Coalition, marking our eighth Medicaid alliance. Under this partnership, we will be initially responsible for providing behavioral health management services with an expansion into a full-risk health management products next year.

As I shared during our last earnings call, our partnership with Blue Cross Blue Shield in Minnesota will go live in the fall of 2018 and serve approximately 375,000 Medicaid and dual-eligible members by the end of the year. We are intensely focused on capitalizing on the pipeline of activity in our Medicaid business. The overall opportunity includes 10 RFPs to be released in the next 18 months and approximately \$80 billion in Medicaid contracts that will be awarded between now and 2022, representing incremental opportunity to our existing business. Much of this opportunity is focused on new and specialized service populations, where Anthem continues to invest and differentiate itself.

As I mentioned earlier, we continue to grow Medicare Advantage business faster than the industry growth rate overall, driven by strong sales performance during the annual election period and throughout the year. We are pleased with our progress and are increasing our investments in 2018 to drive greater membership growth and support continued star-rating improvement. With the addition of America's 1st choice, we now expect to end the year with approximately 900,000 Medicare Advantage lives with more than 70% in 4-star plans. With a total of 5 5-star plans, we believe that our ability to market year round coupled with our enhanced capabilities will help improve our penetration in the market.

We are pleased with the progress in our integration planning ahead of the launch of IngenioRx. We continue to expect to fully migrate our membership on to our new platform by January 1, 2021, and feel very good about the growth opportunities that lie ahead for us with a competitive PBM offering.

Earlier this month, we released our first IngenioRx drug trend report, which summarizes the consolidated pharmacy and medical drug trends for Anthem's affiliated health plans. The report demonstrates unique value that our holistic, integrated approach will bring to the PBM marketplace through our ability to leverage both medical and pharmacy data to reduce drug costs, identify gaps in care and improve compliance and outcomes.

Finally, I want to update you on how we are progressing in our efforts to improve execution across Anthem. On the previous earnings call, I shared my focus on operational performance discipline and the work we're doing to create an agile culture that proactively identifies new opportunities to drive profitable top line growth.

Within the current dynamic health care landscape, we have a unique opportunity to leverage our assets and better serve customer needs by enhancing quality and affordability. Our primary focus is on optimizing our performance within our current business while also creating an organization that can maximize the many growth opportunities we've identified and capitalize on new growth opportunities as they emerge.



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

We will continue to be opportunistic in our approach to M&A. Our recently completed acquisitions of America's 1st Choice and HealthSun are examples of solidifying our market presence in Florida, the fastest-growing Medicare Advantage state. We're also evaluating opportunities that expand our capabilities or broaden our geographic position to better serve our members.

Within our businesses, we're increasing our focus on leveraging the power of our local market presence, which is key to driving change in health care. By combining our best-in-class local market share and our broad capabilities in medical, pharmacy and specialty, we can deliver innovative approaches to ensure our members receive high-quality care in the right setting at the right time. For example, our Anthem Whole Health Connection is an innovative program that leverages Anthem's broad capabilities to provide a holistic approach to care for our Commercial members. Through the program, network providers can access Anthem's medical, pharmacy, dental, vision and disability claim and clinical data, which can help them better diagnose and improve the health of their patients. For example, an eye care provider is able to access clinical data that helps determine whether a patient's eye condition is also linked to other chronic diseases such as diabetes or heart disease. Additionally, we remain focused on improving the overall quality and cost of health care by aligning incentives in the provider community and rewarding the highest quality, most innovative providers.

Anthem has been recognized as a leader in this area through programs like Enhanced Personal Health Care, which was launched in 2012 to support primary care providers in coordinating, planning and managing care for their patients. A recent analysis of our Enhanced Personal Health Care results from 2013 to 2016 demonstrated that we saved over \$1.2 billion of medical cost over the 3-year period. Enhanced Personal Health Care providers consistently delivered better outcomes than a matched group of peers who did not participate in the program. We continue to see growth in this program in both participating care providers and members, with more than 61,000 providers and 5.7 million Anthem Commercial members benefiting from the program's demonstrated value and reducing cost and improving care. We know that in order to provide consumers with high-quality health care and improved outcome, we also need to look beyond traditional health care delivery. Through our integrated care delivery programs and the Anthem Foundation, we are focused on addressing social and societal issues in areas such as housing and food supply, which also significantly impact good health. For example, our CareMore Togetherness Program is the first in the industry to address the growing issue of senior loneliness. The program, which launched last year, provides isolated seniors with weekly phone calls, home visits, transportation and a connection to community-based programs. Through the Togetherness Program, we've been able to close gaps in care and increase participation in CareMore's care centers. Despite the participant's higher comorbidity index scores relative to other members, their admits per 1,000 were 5% lower in year 1, and their total medical costs, 13% lower for seniors participating in this program.

Finally, as you may have noted from the introduction at the beginning of the call, we've made some leadership changes to better align the strength of our executive team with critical opportunities to drive improved execution and growth. First, Brian Griffin has been appointed as CEO of IngenioRx, one of our most important growth opportunities. With more than 30 years of experience and a deep understanding of pharmacy benefit management, Brian brings the leadership skills necessary to build and launch IngenioRx as a transformative PBM offering, with best-in-class capabilities to deliver better outcome and a lower cost of care.

Peter Haytaian is now leading our Commercial & Specialty business. As President of our Government Business, Pete demonstrated his ability to deliver consistent results, with double-digit revenue growth and new Medicaid partnerships. In this new role, Pete will be able to apply his broad operational skill set that did drive growth within the commercial side of our organization.

We are currently conducting a search for a new leader of our Government Business Division. Within the Government Business division, Dr. Tunde Sotunde has been appointed President of our Medicaid business. Tunde has proven to be a strong operator, with extensive Medicaid experience and most recently, led Anthem's north Medicaid region.

Additionally, Marc Russo will continue to lead our Medicare business. Mark has been highly successful in driving our work to rebuild our Medicare Advantage business over the last 4 years.

Dr. Craig Samitt is now leading our newly formed Diversified Business group. Today, Anthem's clinical performance has been driven, in large part, through a collection of medical management, care delivery and analytic solutions represented by our AIM, CareMore, HealthInsight and HealthCore division. We have now unified these businesses under the Diversified Business group umbrella, and we'll invest in this division as a vehicle to enhance Anthem's clinical performance and drive diversified growth. Craig brings more than 20 years of experience in health care delivery and



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

service organizations and is ideally suited to lead our efforts in capitalizing on new sources of growth and deepening our relationships within the health care community.

In addition to the leadership changes on my executive team, we are also implementing a new management structure within our Commercial business that will allow us to better deliver innovative solutions with greater speed to market and accelerate growth. This new structure is organized around our product segment, with a focus on our large group, small group and individual products and will align our product, underwriting and network strategies, consistently driving best practices across all 14 Anthem states and enabling our local leadership team to execute and deliver the most appropriate solutions for our customers.

We will be adding talent across the organization that will help us further capitalize on growth opportunities and execute on our planned investments. As you already know from this call, Chris Rigg has joined Anthem as Vice President, Investor Relations. Chris comes to Anthem after spending more than 15 years as a sell-side equity research analyst covering the health care services industry.

And finally, we recently announced that Rajeev Ronanki will be joining Anthem in the second quarter as our Chief Digital Officer. Rajeev brings more than 15 years of leadership experience in health care and technology, most recently focused on advancing analytics through artificial intelligence. Rajeev will oversee the execution of our digital, artificial intelligence and other the exponential technologies.

To summarize, while we are pleased with our first quarter performance, we know we have more work to do to unlock the full potential of our company, deliver shareholder value and make a meaningful difference in the health care experience for our members.

With that, I'll turn the call over to John to discuss our first quarter financials in greater detail. John?

John Edward Gallina - Anthem, Inc. - Executive VP & CFO

Thank you, Gail, and good morning. As Gail mentioned, our financial performance was strong for the first quarter, with GAAP earnings per share of \$4.99 and adjusted earnings per share of \$5.41, both ahead of our expectations. Our results reflect strong medical management performance across the enterprise.

We ended the quarter with 39.6 million members, a decline of 616,000 members since the end of 2017. Our self-funded membership grew by 333,000 members during the quarter to 25.3 million lives, equating to growth of 1.3% versus the end of 2017. The increase was mainly driven by new account wins in our national and local group businesses. Our fully-insured membership declined by 949,000 members during the quarter, primarily driven by the actions we took last year to reduce our participation in certain individual ACA-compliant markets.

Our individual membership ended the quarter with 755,000 lives, a decline of more than 800,000 versus year-end 2017. Of our remaining members, roughly 500,000 are in ACA-compliant products and approximately 250,000 are in non-ACA-compliant products. Additionally, as Gail mentioned earlier, our large group insured enrollment declined by more than we expected. These declines were partially offset by growth in our Medicare business, reflecting the recent acquisitions as well as strong organic membership growth across our markets.

In the first quarter of 2018, operating revenues of \$22.3 billion were relatively flat compared to our prior year quarter. Revenue results versus the prior year reflect premium rate increases to cover overall medical cost trends and to cover the impact of the return of the health insurance tax in 2018. Additionally, first quarter 2018 revenues include the HealthSun and America's 1st Choice acquisitions, along with the organic enrollment growth in the Medicare business. These increases were mostly offset by the impact of our lower individual, local group insured and Medicaid enrollment.

Our first quarter results benefited from a few retro premium adjustments in our Medicaid business. These are adjustments where we have been proactively engaging with our state partners, and we had expected to receive the adjustments in the second quarter. Fortunately, certain adjustments were received at the end of first quarter, increasing our first quarter results by nearly \$0.20 per share.



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

The medical loss ratio in the first quarter came in at 81.5%, a decrease of 220 basis points from the prior year quarter. The decline was primarily driven by the return of the health insurer tax in 2018. In addition, medical cost performance across our business segments came in better than we had expected, supported by our integrated clinical and care management programs. Additionally, we improved the financial performance in our Individual business as a result of the strategic actions that were taken in 2017, and our results also include the timing benefit from the retroactive revenue adjustments in our Medicaid business.

Our continued focus on deploying effective medical cost of care initiatives across the enterprise is bearing fruit as evidenced by our gross margin results in the quarter. Our strong results include covering the cost of an elevated flu season. Not only did the flu season start earlier than normal, which impacted our fourth quarter 2017 earnings, it also peaked at levels not seen since the 2009, 2010 flu season. Our initial 2018 guidance assumed the impact of a more severe flu season than normal, but flu activity peaked even higher than those estimates in February. Fortunately, flu activity returned to normal levels in early March, which was faster than we had anticipated.

Related to the 2018 medical cost trends. We continue to expect our local group insured medical cost trend to be in the range of 6% plus or minus 50 basis points.

Our first quarter 2018 SG&A expense ratio came in at 15.3%, 100 basis points higher than the 14.3% from the first quarter of 2017. The increase in the ratio versus the prior year was mainly due to the return of the health insurer tax in 2018 and the impact of increased investments spend to support our growth initiatives. Additionally, our first quarter 2017 SG&A ratio was elevated due to the Penn Treaty assessments.

Overall, our results were very strong and slightly better than our expectations. We aggressively managed the impact of fixed cost deleveraging from our reduced footprint in the Individual market and remained disciplined in managing our administrative expense, while funding a meaningful increase in our investment spending.

So now turning to the balance sheet. As in the past, we have included a roll forward of our medical claims payable balance in this morning's press release. For the first quarter of 2018, we experienced favorable prior year reserve development of approximately \$650 million, which was moderately better than expected. Our reserves continue to include a provision for average deviation in the mid- to high single digits, and we believe our reserve balance has remained consistent and strong as of March 31, 2018.

Our Days in Claims Payable was 40.3 days in the first quarter, an increase of 0.9 days from the 39.4 days we reported at the end of 2017. We continue to believe that our DCPs will be in the high 30s over time.

During the quarter, we reported just 1.7 million shares of our outstanding common stock for \$395 million at a weighted average price of \$223.51 per share. We also used \$192 million during the quarter for our cash dividend. And yesterday, our audit committee declared a second quarter dividend of \$0.75 per share.

Our debt-to-cap ratio was 42.4% at the end of the first quarter, a decrease of 50 basis points from the 42.9% we reported as of the fourth quarter 2017. We continue to expect a decrease of debt-to-cap ratio towards the low 40s.

During the quarter, we raised approximately \$850 million from the debt markets. The additional debt, along with cash on hand, was used for the purchase of America's 1st Choice, the repayment of \$625 million of debt that matured in the quarter, share repurchases and the payment of ordinary dividends and interest expense in the quarter. As a result, we ended the quarter with cash and investments at the parent company of \$1.1 billion, a decrease from the \$2.8 billion we reported in the fourth quarter.

And finally, our operating cash flow during the first quarter was \$2.2 billion or 1.7x net income. Cash flow in the quarter included the impact of collecting an extra CMS Medicare payment and also the fact that we did not make an estimated federal tax payment. As a reminder, we will make 2 estimated tax payments to the federal government in the second quarter. Overall, first quarter operating cash flow was in line with our expectations.

Turning to discuss our high-level expectations for the remainder of the year. We continue to expect our fully insured enrollment to be in the range of 14.8 million to 14.9 million members by the end of the year, reflecting higher Medicare Advantage enrollment from America's 1st Choice, offset



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

by the lower-than-expected membership in our local group insured business. Self-funded membership is now expected to be in the range of 25.3 million to 25.4 million members, an increase of 100,000 members from our previous outlook, driven by better-than-expected enrollment in BlueCard. In total, we now expect medical membership to end the year within a range of 40.1 million to 40.3 million lives, relatively flat from where we ended 2017, which means we successfully replaced the lost membership from our reduced footprint in our Individual ACA-compliant markets.

Operating revenue is now expected to be in the range of \$91 billion to \$92 billion, an increase of \$500 million at the midpoint from the prior range. The increase is driven by the addition of America's 1st Choice, partially offset by lower-than-expected enrollment in our local group insured products.

We now expect our consolidated medical loss ratio to be 84.4% plus or minus 30 basis points, a 10 basis point improvement at the midpoint from our previous expectations. Our updated medical loss ratio reflects the better-than-expected medical cost performance in the first quarter across the enterprise.

The SG&A ratio is now expected to be 15.4% plus or minus 30 basis points, a decrease of 10 basis points at the midpoint, as the mix of our operating revenue profile is more weighted with revenues that have a lower-than-average administrative expense ratio.

We continue to expect 2018 operating cash flows to be greater than \$4 billion. Taken together, and reflecting our strong first quarter and positive outlook for the remainder of 2018, we now expect our full year 2018 GAAP earnings per share to be greater than \$14.12 and adjusted earnings per share to be greater than \$15.30.

And with that, I'll turn the call over to the operator for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question today comes from the line of A.J. Rice with Crédit Suisse.

Albert J. William Rice - *Crédit Suisse AG, Research Division - Research Analyst*

Congratulations, Chris, on the new role there. Just thanks, again, Gail, for laying out all those initiatives and priorities that you have. I wondered, when you think about capital needs and where you're going to direct capital, do those initiatives require much capital? Do they change your thinking on capital uses? John, I don't know if you affirmed the \$1.5 billion buyback target. Is that still the target? And then sort of a variation on the priorities and initiatives aspect, also ask you about industry consolidation, how that's factoring into your strategy? Obviously, other people's consolidation, I guess I'm more thinking about of, does that change any priorities for you?

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Great. Thanks for the question. There's a couple of things embedded in your question, so let me start, and then I'll ask John also to comment on capital. We're -- Our capital priorities have consistent to what I shared in the fourth quarter call, which is a balanced approach to dividends and buybacks as well as continuing investments in our -- on our own business, and we see a number of opportunities, as I've shared, that we are continuing to invest in: the modularization of our product capabilities, consolidation of our systems and platforms. We're also investing in our digital capabilities to respond -- to provide more personalized and responsive support. And so we see these as the -- a couple of the investments as well as the continued investment in how we work with the -- our care providers across integrated delivery opportunities. So I guess I would answer your overall question with our capital deployment priorities are pretty consistent. On the M&A front, as I shared in my comments, we are certainly opportunistic, as we were with the 2 Medicare Advantage assets that we recently purchased, which are high quality and, we think, help us provide a much deeper penetration into our Medicare Advantage business. And we also are opportunistic about capabilities that, we think, can help drive the growth opportunities across our business. From an industry consolidation standpoint, we feel we've got significant growth opportunities



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

in terms of our own business. The launch of IngenioRx provides us with some really significant growth opportunities over the next several years, and we think that's going to resonate very strongly in the marketplace. And as I've also shared, I think, across the Medicaid space, significant pipeline of specialty, different specialized populations as well as core growth, Medicare, again, we're investing in the space and have continued to invest in the space, still very positive about it. And I also do believe that we have opportunity, as I've shared, in our Commercial space, as we improve our execution at the Individual market level. I'll ask John, maybe, to make some additional comments given that.

John Edward Gallina - *Anthem, Inc. - Executive VP & CFO*

Yes. Thank you, A.J. So I'll just -- on the share buyback, yes, we do intend to still buy back approximately \$1.5 billion during the year. If you look at our first quarter results, we're a little bit north of 1/4 of that associated with the actual buyback that has occurred so far in the first 3 months of the year. And on the capital deployment, as Gail said, we want to be opportunistic, and we also want to be very capital efficient. I don't know that there's a better example of standing up a new line in the capital efficient manner than how we're handling the IngenioRx rollout. I mean, we're going to stand up our own PBM in the most capital efficient manner within the industry and feel very, very good about that and then, you take the other capital that we have in terms of being opportunistic. We think we can really deploy it very wisely over the next few years.

Operator

And we do have a question from the line of Ana Gupte with Leerink Partners.

Anagha A. Gupte - *Leerink Partners LLC, Research Division - MD, Healthcare Services and Senior Research Analyst*

So your MLR is looking great. You've improved your guidance. Your operating margin expansion is great. It sounds like, of course, the fully insured just generally remains pressured for the industry. As you look forward into 2019, do you think we could see your MLRs and margins sustainable while you still grow membership just because it looks like your medical's cost structures improving, you may get more specialty penetration, does this delay or might we see some compromise on the margins business membership?

John Edward Gallina - *Anthem, Inc. - Executive VP & CFO*

Yes. This is John. So thank you for the question. In terms of where the MLR, we're very pleased with the performance that we have here in the first quarter, and I believe that our outlook and increasing guidance by \$0.30 to greater than \$15.30 actually helps us solidify the sustainability of that. Yes, as we look to 2019, it's a little premature to provide specific information associated with metrics, but what I will say is that when we price, we will price in a disciplined manner. We'll price based on our target margins, which are determined on a pretax basis and feel very good about the fact that we have a good sustainable platform in order to grow our business.

Operator

And we do have a question from the line of Steve Tanal with Goldman Sachs.

Stephen Vartan Tanal - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

I guess just a bigger picture question, maybe, for you Gail. On the last call, you sort of reiterated a commitment to a long-term EPS growth algorithm of high singles to low double digits. And I guess your optimism toward moving to the higher end of that range, of course, there is some of your competitors that have higher growth rates out there but granted with a different mix of business. And so I guess, what I'm trying to understand is what would it take to sort of reset that algorithm higher? And should we assume that some of those specific actions are part of your longer-term plan?



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Well, thanks for the question, Steve. What I shared with everyone at the last call was, we feel very optimistic about our business. There's a number of things inside of our business, which I've already outlined, and we'll go through them again, but the growth opportunities -- the organic growth opportunities plus the growth that standing up in -- of IngenioRx brings to us, I think, provide us a lot of confidence around moving from high single to low double digits, at the higher end of that range. So I'm not going the comment beyond that, but I would say that across our leadership team and the work that we're focused on, which is clearly executing on our opportunities, we always aspire to do better, but we're intensely focused on delivering on the commitments that we've laid out.

Operator

And we do have a question from the line of Dave Windley with Jefferies.

David Howard Windley - *Jefferies LLC, Research Division - Equity Analyst*

Gail, this one is around, kind of, your -- changing your organizational structure and go-to-market strategy in the service areas. I've heard you talk before and today about preparing that IngenioRx PBM business for external sales. What other services do you envision potentially being able to go to market and provide to, say, Blue sisters or other plans? And again, within the organizational structure change, are those going to be attached to or folded into IngenioRx in some way? Or just thinking about -- how you plan to go to market with that?

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Great. Well, thank you for the question. There's a couple of ways to look at it. IngenioRx, by itself, is a significant opportunity for us to sell a -- I think a new model PBM, so we've shared that opportunity, but in addition to that on the call today, talking about our Diversified Business group, we have historically had a number of companies and assets that we are looking to leverage more extensively. Assets like AIM and CareMore, or HealthInsights, or HealthCareAnalytics, Payment Integrity, those are assets that, first and foremost, we deployed inside of Anthem to help deliver many of the medical cost results that we've had. Provider Enablement and tools, the Enhanced Personal Care initiative that I shared with you is another example of not just contracting methodologies but data informatics and tools and supporting care providers at the market level. What we're doing is really bringing those together. First and foremost, we're focused, and we think we do have an opportunity to sell those to other plans within the system and also do partnerships with them. I think the Medicaid partnerships are great example of our goal, I think, to help leverage our assets to help this overall system, and we think that we've got some very strong capabilities there. But it's also, I think, beyond the Blue system working with care providers. In their system, I think, we've got opportunities to sell into that as well. So it's a fairly broad strategy. We've just brought those asset together, so at this stage, it's an emerging component, but it's something that already provides us support inside of our business.

Operator

And we do have a question from the line of Kevin Fischbeck with Bank of America.

Kevin Mark Fischbeck - *BofA Merrill Lynch, Research Division - MD in Equity Research*

Wanted to ask a strategic question about the deals that are going on around here. I guess, there's 2 things, I guess, that I'd like you to respond to, but the first one is, this perception that some companies have decided to kind of there to build or is there, buy capabilities to get the benefits of what they're doing. I understand that you think that you can build things through IngenioRx but obviously, there's a time difference and potentially buying something that's already there in place and working well versus building something out and improving out that concept, so I want to get your thoughts around that. And the second part really being the cash flow impact of these transactions when I look at United from a free cash flow basis doing \$13 billion and CVS-Aetna doing \$12 billion. When I think about free cash flow to parent, Anthem is going to be maybe 1/4 of that size



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

or 1/3 of that size, so how do you think about your ability to kind of compete for the next round of deals or next round of capabilities, given your competitors are getting much bigger?

Gail Koziara Boudreaux - Anthem, Inc. - President, CEO & Director

Kevin, thanks for the question. Let me address the strategic opportunities, and then I'll have John speak to a little bit of the cash flow impact. First and foremost, I think John stated it particularly around the PBM, we're going to be able to build an incredibly cash-efficient, capital efficient PBM by leveraging the buying power of our partner, CVS, in this. We're going to put into the market sort of all new capabilities essentially, and I think from that perspective, we feel that we're advantaged, that we have an opportunity to build the next-generation PBM, with brand-new technology and at scale. and not only across our business but an opportunity to sell that into other businesses. More broadly, as we think about M&A, one of the unique things, I think, for Anthem is our deep market presence, and we have significant organic growth opportunities inside of our own business that we're going to leverage and take advantage of, but we also have opportunities because of our scale and local scale to do partnerships, and again, more effectively leveraged capital in the most efficient way. So I think that our overall strategy, yes, we'll be opportunistic particularly around capabilities and areas that we think will help us grow our business faster, but we have a very strong view of where we believe that our growth profile can come from and the positive returns that we can have. So with that, I'll ask John to more specifically address your question around on overall capital.

John Edward Gallina - Anthem, Inc. - Executive VP & CFO

Yes. Thank you, Kevin, for the question. In terms of our cash flow and cash availability at the parent, we do have, we believe, enough dry powder available given our size and our scale. As Gail said, we want to be opportunistic about M&A, solidify our expanded footprint, enhance merit capabilities, basically whatever we need to do to serve our members better, and we'll look at M&A in that capacity and believe that we are not at all disadvantaged in terms of our ability to finance a potential acquisition. We don't want to do the -- do a deal for the sake of doing a deal. We want to do a deal to help serve our members better, and we need to make sure that we keep that in mind, as we go forward and look at these potential opportunities.

Operator

And we do have a question from the line of Josh Raskin with Nephron Research.

Joshua Richard Raskin - Nephron Research LLC - Research Analyst

Congrats to Chris as well. First question -- I guess, my question here. You'd made some comments about a month ago around cadence of earnings this year and then applied something here no north of \$4.50 in the first quarter, did more than \$0.90 above that. I heard the \$0.20 of timing related to the Medicaid retro payment, so maybe it's only \$0.70 of upside. I just want to -- I just that would be, with the guidance going up by \$0.30, I didn't hear anything sort of negative or offsetting or even worrisome in the commentary. Was there a big sort of acceleration in investments or something else that we should be thinking about, a change in seasonality or something else that you noticed? And then, if I could sneak in a quick follow-up, can you use America's 1st Choice, that 5-star plan, can use that to expand your footprint through plan consolidation? Is that actually a strategy you're going to use to have more 5-star plans or larger geographies under 5-stars?

John Edward Gallina - Anthem, Inc. - Executive VP & CFO

Sure, Josh. I'll take your first half of your 1 question, and then turn it over to Gail for the second half. Right, in terms of seasonality and guidance, you're correct. About a month or so ago, we talked about the fact that a year ago, we earned a little more than 2/3 of our earnings in the first 6 months of the year, and the expectation here in 2018 is that it would be just over 60% -- slightly greater than 60% would be earned in the first half of the year. And then, a little bit more than half of that would be earned in the first quarter. And when that was made, there were a couple of things, you've identified the \$0.20 timing issue associated with the Medicaid retro premium adjustments, where -- that's a great thing, we got the early.



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

That clearly just moves money from the second quarter to the first quarter. In terms of our expectations, doesn't really change the overall annual structure. The other part was the flu season. We had anticipated a worse-than-normal flu season. It started in December, and our guidance baked that in. And through the end of February, it was quite elevated, and we expected it to be elevated through the end of March. And quite honestly, the month of March was a more normalized flu season. And so that in and of itself created a benefit to the first quarter more so than we were expecting. And then really, and probably most important is the strong underlying results, better-than-expected MLR, really a strong medical management-type initiatives and success in that area. And all those things I'll equate it to really a very, very strong first quarter. We still believe that for the first half of the year that our earnings expectations is that it will be a greater than 60% of the annual number, but as you pointed out, it is a little bit different between the first quarter and the second quarter than maybe we anticipated 30 days ago.

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Josh, in terms of your second question. Just a couple of points. One, as I indicated earlier in my comments, we do have 5 5-star plans, and 2 of those 5-star plans are already in the Florida marketplace. So we feel -- we obviously have good growth potential they, and as you probably know, CMS is also changing that rule round consolidation, so our expectations don't include the need to engaged in that strategy. It's not a strategy that we've deployed as much I think as some of the others. And then a third point really, we are a little bit unique in that we do grow quite a bit through the SEP process with our dual products, so we feel that there is strong growth opportunities throughout the year in our Medicare Advantage plan.

Operator

Your next question comes from the line of Justin Lake with Wolfe Research.

Justin Lake - *Wolfe Research, LLC - MD & Senior Healthcare Services Analyst*

Gail, you talked about the loss of employer group risk membership being driven by Anthem's relative lack of introducing more affordable products to allow employers to offset the return of the health insurer fee. So let me just apologize upfront for the long way of question, but given all the focus on the commercial pricing environment I want to make sure we understand what you're saying here. Can you talk to the '18 pricing environments, specifically around what types of competitive products you're talking about that are driving the share shift? For instance you're referring to, like, the level funding products about I hear out there. And specifically, did you see competitors cutting price or not fully passing for the HIF on like-for-like products, and thus getting cutting margins? Or was this mainly product-driven? And then finally, where do you expect to end the year on Commercial employer group risk membership and share any color you can on the new product you're planning to introduce to the market and the timing of those products.

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Thanks, Justin. A very fulsome question there, so I'll attempt to go through pieces of it, and then, I'll also ask Pete Haytaian to comment, because he has been out in the market. Well, let me start with sort of the overall environment. Fully insured market has always been competitive, and I still believe in, it is rational. What I shared is that we did price to the full extent, full impact of the health insurers fee in the marketplace, and we saw a greater percentage of employers converting to self-funded. That was one issue. And the second one, I think, is more of Anthem-specific where in terms of execution at the sales level, we did not offer a fulsome set of buydown opportunities for our employers. That's an area that we recognize. We're disappointed in it, but we also believe that we can offer -- we have a portfolio of products. We have 2 things that we're doing. One, is we are -- have been investing heavily in getting product to market faster through this modularization process as well as enhancing and expanding what we have in the marketplace right now, and a lot that is around affordable options for employers as the health insurance fee increased pricing more than it had in the past. The second is, as part of our segment strategy, getting information more quickly back so that across our 14 markets, we can make sure that we're deploying those strategies consistently in best practices. So that's how I would say the market evolved for us. We do think that we have an opportunity going forward to improve that execution. That's an area that Pete has been specifically focused on. I'm going to ask him to probably provide some commentary for you. Pete?



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

Peter David Haytaian - AMERIGROUP Corporation - Former CEO of Northeastern Region, CEO & President of Amerigroup New Jersey Inc

Justin, thanks for the question. I don't want to repeat everything that Gail said. I think with respect to products and options and network configuration, we definitely have additional opportunities. I've been in the markets now for about 4 weeks. I'm doing pretty detailed business operating reviews for the last 4 weeks. I'm encouraged by the opportunity, but I'll say this very directly. I think this is really a matter of execution more than anything, quite frankly. While we can bring more products and services to the marketplace and network configurations, I think what Gail mentioned is critically important, and that is the segment model, in which we are going to be sharing best practices across the organization in a consistent manner. Standing up a sales effectiveness organization, we are going to have tools and capabilities that are going to drive consistent growth right down to the account manager and rep level. Underwriting being intertwined and really connected with all that. And then, leveraging our market relationships and our deep understanding of the market and provide the relationships. So it is a matter of execution. I'm encouraged by it. I think if we line that all up effectively with some of the new products and services and network configuration that Gail mentions, we'll be very successful in the marketplace.

Operator

We do have a question from the line of Zach Sopcak with Morgan Stanley.

Zachary William Sopcak - Morgan Stanley, Research Division - VP on the Healthcare Services and Distribution Team

I just wanted to go back to the medical loss ratio coming in better than you expected for the quarter. It sounds like flu netted out a slightly better than you thought. Was there anything else in underlying utilization trends of -- endemic to the environment that helped impact that number? Or was it purely medical cost management? Anything specific that you can talk about the medical cost management side that seems to be working?

John Edward Gallina - Anthem, Inc. - Executive VP & CFO

Sure, Zach. Flu clearly was a contributor. Overall, it really was a good disciplined pricing with strong medical cost management across the enterprise. I will say that our Individual business actually did a little bit better than expected as well. The strategy that we employed with our reduced footprint actually is playing out extremely well and that helped, but it's really -- it's across the board, where we're actually pretty excited about the long-term prospects now.

Gail Koziara Boudreaux - Anthem, Inc. - President, CEO & Director

Yes. And I'll add to the John's comments. I would not point to one specific program. We've had a very comprehensive set of initiatives across integrating care providers, enhanced personal care, additional unit cost. I mean, Payment Integrity, we've invested over the last few years in that, and that's an area with, also, the alignment of our teams in this regional structure. We're now focused with our contracting clinical teams across all of our businesses. And I think that intense focus is also paying off for us, so I would not point to one specific thing, but I think it's an ongoing focus on managing medical costs effectively for our customers and being a good steward of their dollars.

Operator

And our next question comes from the line of Ralph Giacobbe with Citi.

Ralph Giacobbe - Citigroup Inc, Research Division - Director

Just wanted to go back to Commercial and sort of the shift from risk to ASO. I think you'd mentioned that was partly due to HIF. With HIF sort of going away next year, would you expect some of that risk business to come back? Or are smaller employers are just sort of not that nimble? And



APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

then as it relates to sort of the business and the shift, did you -- was it sort of shifted to ASO meaning that you retained it, or did you just lose it to a competitor sort of moving from risk to ASO?

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

We -- Ralph, thanks for the question. Let me try to kind of walk you through each of the individual pieces. In terms of the shift to ASO, I am still and our team is still very optimistic quite frankly about our opportunities in the fully insured space and clearly, not having the health insurers fee in 2019 will be a positive overall for our ability to provide affordable products in the marketplace. So yes, we're -- we think there's opportunities in fully insured space. Thinking about the conversion of self-insured, essentially, we retained a portion of it. Certainly, a significant portion of that moved to our self-insured business, and we were able to add additional services, our dental life, clinical programs, et cetera in that space, but we did lose a portion, as you can see, just from the overall numbers, and that's an area that Pete, I think, was very direct about, an area of execution that we think that there were other opportunities for us to impact our persistency and keep those clients Blue. We will, obviously, be working very hard to get those customers back. The market is competitive. It's dynamic. And employers, we have a very strong brand reputation. And I think very strong loyalty in the market, and so that'll be part of a win-back campaign that we put into the marketplace.

Operator

And we do have a question from the line of Peter Costa with Wells Fargo Securities.

Peter Heinz Costa - *Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

As you grow your Government Business and you look at your competitors in that space that are more substantial in the Government Business, several of them are acquiring health care service companies or providers. Is that a direction you see yourselves moving towards in the future? And compare that and contrast that, if you would, with the multidistrict Blue Cross Blue Shield litigation against the Blues plans. Does that make that -- does that actually help you to acquire providers if that's a direction you're going to go in?

Gail Koziara Boudreaux - *Anthem, Inc. - President, CEO & Director*

Peter, I'm not going to comment on ongoing litigation. But what I would say about the acquisition of plans and primary care, part of our acquisition for HealthSun, for example, in our Medicare Advantage assets in Florida, we do have clinics, and they are integrated. We also own CareMore, which is a large part of our strategy around not only Medicare but also Medicaid. And a wraparound Primary Care Plus. Also primary care models that we're putting into the marketplace, so we do own assets in the Government Business that support that. But I think I've shared this before, we also believe that because of our market share and strict or the tight alignment that we have with care providers, that we can build great partnerships with them through contracting, through integration, through providing them tools. And what makes it a little different for us is our market share across these markets enables us to do that, and as you saw it from even the Enhanced Personal Care results, we're seeing a lot of traction in that model, so we're very interested in wrapping around things for the home and providing them other services, which we do as part of our AIM subsidiary as well and some of the other work going on in Diversified.

Operator

And our last question of the day comes to the line of Gary Taylor with JP Morgan.

Gary Paul Taylor - *JP Morgan Chase & Co, Research Division - Analyst*

Just a couple of follow-ups on IngenioRX. First, you talked about the capital efficiency of setting this up, which, I think, is mostly an acknowledgment that you're not spending tens of billions of dollars to acquire the capabilities. Could you just review for us what capital commitments, if any, you

APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

have in '19 and '20 for this? And then also, on the G&A side, is there a material step up in the G&A investment in '19 and '20 as you set this up? And if so, does that mean 20% of the gross benefits still flowing down to earnings is the expectation?

John Edward Gallina - Anthem, Inc. - Executive VP & CFO

Gary, thank you for the question. I'll just say at first, in terms of the capital commitments we have associated with Ingenio for setting up in '19 and '20, it's quite minimal. And the guidance that we've provided and the long-term growth rate that we've provided has already encompassed whatever additional spending that might need to be incurred in order to set it up successfully. So we're pretty comfortable with that. And then in terms of just G&A in general, over the next few years, there's always moving parts every year. We have increased our investment spending quite significantly here starting in late 2017 and moving into '18, as we really want to focus on growth opportunities and enhancements and things that can serve our members better. And we'll obviously reassess that on an annual basis but there's nothing that's truly significant and meaningful that will impact your modeling of it. With that, I want to turn your question over to Brian Griffin, who can give you a little bit more color in terms of some of the capabilities that we're building.

Brian Thomas Griffin - Anthem, Inc. - Executive VP & CEO of IngenioRX

Thanks very much, John. So as John indicated, I think that as we evaluated our next step in our strategy with respect to the launch of Ingenio, we were focused on optimizing the value, obviously, that we'd be in a position to create for our clients and consumers. I think importantly, just to add to John's comments, what is very important about this is that we are launching our own PBM. And with that, importantly, we have control over all of the key financial levers. So I think, as John indicated, in terms of new capabilities, we're going to be in the position to have a complete control over the design of our pharmacy networks. We, today, have control, although all of our formulary and clinical programs, and as we think about relationships with Pharma, we'll be in the position to negotiate directly with Pharma to create new business relationships. So that puts us in the position of having a whole new set of capabilities that can't believe we don't have today. Obviously, we're very excited about it. And Gail in her introductory comments pointed to the integrated value propositions that we're going to market with, and we see the market responding very well to that value proposition. Just 2 weeks ago, we had our inaugural client forum, and I think that there's a lot of enthusiasm, particularly around -- among our medical clients, so that's government labor, our national accounts. But importantly, also within the Blue Cross Blue Shield system, there's significant interest in us being able to provide them an integrated value proposition themselves. And so I think, we'll see a lot of excitement within that part of the industry as well.

Gail Koziara Boudreaux - Anthem, Inc. - President, CEO & Director

Thank you, Brian. And thank you all for joining us this morning. We're very excited about the opportunities that lie ahead of us. We are intensely focused on improving execution throughout our company, delivering on the significant growth opportunities within our existing business and creating an agile, innovation-focused culture that can identify and capitalize on new growth opportunities in what continues to be a dynamic health care market.

And I want to thank each of our more than 58,000 associates for their commitment to Anthem and for living our values each and every day to deliver on our promises to always serve. Thank you for your interest in Anthem, and I look forward to speaking with you at future events.

Operator

And ladies and gentlemen, this conference will be available for replay after 11:00 a.m. today through midnight. You may access the AT&T Teleconference Replay System at any time by dialing 1 (800) 475-6701 and entering the access code 432033. International participants may dial (320) 365-3844. That does conclude your conference for today. Thank you for your participation and for using the AT&T Executive Teleconference service. You may now disconnect.

APRIL 25, 2018 / 12:30PM, ANTM - Q1 2018 Anthem Inc Earnings Call

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2018, Thomson Reuters. All Rights Reserved.