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HUM.N - Q4 2021 Humana Inc Earnings Call

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OVERVIEW:

Co. reported 4Q21 adjusted common diluted EPS of $1.24. Expects 2022 adjusted common diluted EPS to be at least $24.

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PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Humana Fourth Quarter Earnings Call. (Operator Instructions) Please be advised today's conference may be recorded. (Operator Instructions)

I'd now like to hand the conference over to Lisa Stoner, Vice President of Investor Relations. Please go ahead.

Lisa M. Stoner - *Humana Inc. - VP of IR*

Thank you, and good morning. In a moment, Bruce Broussard, Humana's President and Chief Executive Officer; and Susan Diamond, Chief Financial Officer, will discuss our fourth quarter 2021 results and our updated financial outlook for 2022. Following these prepared remarks, we will open up the lines for a question-and-answer session with industry analysts. Joe Ventura, our Chief Legal Officer, will also be joining Bruce and Susan for the Q&A session.

We encourage the investing public and media to listen to both management's prepared remarks and the related Q&A with analysts. This call is being recorded for replay purposes. That replay will be available on the Investor Relations page of Humana's website, humana.com, later today.

Before we begin our discussion, I need to advise call participants of our cautionary statement. Certain of the matters discussed in this conference call are forward-looking and involve a number of risks and uncertainties. Actual results could differ materially. Investors are advised to read the detailed risk factors discussed in our latest Form 10-K, our other filings with the Securities and Exchange Commission and our fourth quarter 2021 earnings press release as they relate to forward-looking statements and to note in particular that these forward-looking statements could be impacted by risks related to the spread of and response to the COVID-19 pandemic.

Our forward-looking statements should therefore be considered in light of these additional uncertainties and risks, along with other risks discussed in our SEC filings. We undertake no obligation to publicly address or update any forward-looking statements and future filings or communications regarding our business results. Today's press release, our historical financial news releases and our filings with the SEC are also available on our Investor Relations site.

Call participants should note that today's discussion includes financial measures that are not in accordance with generally accepted accounting principles or GAAP. Management's explanation for the use of these non-GAAP measures and reconciliations of GAAP to non-GAAP financial measures are included in today's press release. Finally, any references to earnings per share, or EPS, made during this conference call refer to diluted earnings per common share.

With that, I'll turn the call over to Bruce Broussard.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Thank you, Lisa. Good morning, and thank you for joining us. Today, Humana reported financial results for the fourth quarter of 2021, reflecting the strength of our core operations, which continued to perform well throughout 2021 despite the challenges the industry faced as a result of the pandemic.

With that in mind, and as we enter a new fiscal year, I want to take a moment and speak not only to our 2021 results and our outlook for the current year but more broadly about our strategy and the steps we're taking to position Humana for success. Susan will discuss our results and outlook in more detail in a moment.

But at a high level, our 2021 results and our 2020 outlook are largely in line with recently provided guidance. Adjusted earnings per share for the full year were $20.64, which was above our previous estimate of approximately $20.50. This represents growth of 11.6% off of our 2020 baseline of $18.50 while covering a $1 unmitigated net COVID headwind. Looking forward, we provided full year adjusted earnings per share guidance of at least $24. This represents 11.6% growth over our 2021 baseline of $21.50 and 16.3% growth of our actual adjusted EPS of $20.64. This guidance includes an embedded COVID headwind of $1.

Before I highlight some of the actions we're taking to deliver improved individual Medicare Advantage membership and how we're applying learnings from the most recent annual enrollment season, I want to emphasize that we are operating from a position of strength. I'm incredibly proud that Humana is the second-largest Medicare Advantage plan provider, supporting over 5 million beneficiaries with high-quality coverage.

The quality of our product offering is the highest among our public peers with over 97% of Medicare Advantage members in plan with a 4-star rating or higher. We've also increased the number of contracts that received a 5-star rating from 1 contract in 2021 to 4 contracts in 2022, which is the most in our history. Finally, we saw an improvement of 930 basis points in our Net Promoter Score this past year, reflecting our ongoing efforts to enhance the customer experience.

We continue to advance our customer segmentation efforts, developing plans that are tailored to the unique needs of our specific member populations. This allows us to provide benefits that enhance and complement an individual's existing coverage through programs like Medicaid or entities such as Veterans Affairs. We're seeing great success through our initial segmentation efforts, growing D-SNP membership greater than

40% in both 2020 and 2021. In addition, our Humana Honor Plan designed for veterans that is also available to all Medicare eligibles grew membership 80% last year.

We have a strong brand and our expertise caring for people as they age is highly recognized by consumers. As a result, we've increased market share over time, achieving annualized enrollment growth of 11% since 2017, which is well above market growth. Moreover, we have a proven track record of balancing membership and margin growth with our long-term earnings growth target range of 11% to 15% continuing to be the ultimate goal.

With that in mind, a key element of our plan is to return to industry-leading membership growth without negatively impacting earnings growth. We will achieve this by leaning into our successful history of reducing costs and improving operational efficiencies. We are committed to delivering sustainable cost reductions in order to create the needed capacity to improve our competitive positioning. We are committing to drive $1 billion of additional value for the enterprise through cost savings, productivity initiatives and value acceleration from previous investments. This will create the capacity to fund growth and investments in our Medicare Advantage business and further expansion of our health care service capabilities.

These efforts span several areas. First, we have already begun a critical review of our ongoing strategic initiatives across the company. We intend to further focus our investments on those priorities where we have the greatest conviction of significant value potential. We will slow or pause further investment in some areas in order to focus on accelerating value creation from investments we've already made.

Next, we will drive further organizational efficiencies by optimizing our workforce in order to speed these -- increase the speed, agility and pace we must work at as a large integrated health care organization. We see the opportunity to streamline our operating structure, standardize work and simplify certain processes to eliminate low-value work.

Third, we will reduce and optimize third-party spend. In some areas of our business, this will translate to decrease in vendor use while in others, we will outsource work to best-in-class suppliers. In addition, with the ongoing reality of COVID and the way it has changed the way everyone works, we will be significantly rationalizing our real estate portfolio.

And finally, we are driving greater operational efficiencies across the organization by modernizing, streamlining and improving our processes through automation and digital advancement. This includes the use of technology to replace manual efforts in our core operations and to increase productivity of our workforce.

Beyond creating capacity to invest in our Medicare Advantage products, we are also focused on optimizing our marketing spend and sales channels to maximize growth. As we've discussed previously, we have undertaken significant work each year to determine the optimal level of marketing investment and how these dollars are put to work. Applying our learnings from the most recent selling season, we expect to further optimize our investment in marketing to ensure our messages are heard by more prospective customers.

We also plan to accelerate digital capabilities to increase our effectiveness and efficiency in member acquisition and focus on experience of our existing members to improve retention. We will continue to focus on ensuring we have a clear differentiated and omnipresent brand with a strong call to action that supports industry-leading customer acquisition. And as we improve the value proposition of our plans, we believe we will see even greater returns from our marketing spend.

Regarding our sales channel, we will look to optimize the use of our internal channels as well as external partners. Our 2,400 employed sales agents work to create long-term relationships with our members, ensuring they are educated on their plan choices and the benefits and additional support services each plan offers. This leads to better engagement, greater plan satisfaction and ultimately, better health outcomes and longer tenure with Humana.

We do not expect significant shifts in channel mix this year. We will continue our efforts to improve retention of our members broadly. This will include a particular focus on those enrolled in third-party call centers, where we've seen term rates approximately 400 basis points higher than our internal call sales channel. We'll be working with our call center partners to more closely replicate the experience delivered by our employed agents through enhanced training and service-level agreements. And we'll also look for opportunities to create greater retention and quality incentives for sales partners.

As I mentioned a few moments ago, Humana offers superior quality to its members, has a strong brand and a long history of expertise in caring for people as they age. Additionally, our clinical focus and suite of health care service capabilities allow us to take a holistic approach to supporting members, ensuring they receive high-quality, proactive and comprehensive care, which improves health outcomes. We will leverage the strength of these core fundamentals as we work with our internal and external partners to improve retention.

As we look ahead and focus on our core operations, we are committed to continuing the track record of being capital-efficient as we consider strategic advancement and return of capital to shareholders. To that end, we are committed to advancing our plans to divest a majority interest in our hospice business as we are confident we can deliver the desired experiences and outcomes for patients transitioning from restorative care to the hospice through partnership models.

We have continued to explore various alternatives for the long-term ownership structure of the business and have initiated steps to reorganize the hospice business for stand-alone operations while also making investments to improve clinician recruiting and retention to position the business for further growth. While we're not able to share details today on a specific transaction structure or timing, we expect that we will be in a position to provide a meaningful update by our first quarter call.

Our ability to drive innovation and improved clinical outcomes is enabled by our strong integrated care delivery platform. And in recent years, we've made significant -- have significantly expanded our health care service capabilities in order to better serve our members and strengthen our payer-agnostic care offerings. Our health care service businesses are an important component of our strategy and will contribute considerably to Humana's long-term growth.

Combining our leading Medicare Advantage platform and growing pharmacy, primary care and home services increases our total addressable market and creates the opportunity for improved clinical outcomes, lower cost of care and increased enterprise margin from our health plan members. Our PBM, which is the fourth-largest in the country, processed 515 million 30-day equivalent scripts in 2021, an 8% increase year-over-year.

In addition, our pharmacy dispensing business continues to deliver industry-leading mail order penetration. And we've successfully implemented tools to enhance our e-commerce experience while expanding our mail order footprint as we get closer to the customer. Our success is not only expanding volume but improving health outcomes, evident by our 4-star level performance in medication adherence metrics, which are 3x weighted.

In our primary care business, we are in the early stages of growth and continue to expand our geographic presence. We are committed to funding the organic growth of our primary care organization in 2023 and beyond through a combination of on- and off-balance sheet such that we expect no dilution to earnings growth from the organic growth expansion.

To provide more insight into our primary care organization, we ended last year with 206 centers, representing a 32% increase over the prior year. We are accelerating the build-out of our platform through a combination of de novo expansion and inorganic growth. We completed 9 acquisitions last year, bringing 40 newly wholly owned centers to our portfolio. We also opened 15 new de novo centers and consolidated 5 clinics into other locations.

We plan to continue prioritizing tuck-in acquisitions focused on the markets where we have established presence to provide more access and high-quality care to patients. In addition, we recently announced our intent to build an additional 26 centers this year under our existing joint venture with Welsh Carson. When combined with planned acquisitions, this is expected to increase our center count by approximately 20% and bringing our total center count to approximately 250 centers by the end of this year.

As we look to 2023 and beyond, we plan to build and acquire an additional 30 to 50 centers per year, again financed in a way that is not expected to be dilutive to earnings. I would remind you that each mature center is projected to drive annual EBITDA of $2 million to $4 million, highlighting the meaningful opportunity, increased contribution to enterprise earnings going forward.

Turning to the home. We recently announced the appointment of our new home leader, Dr. Andy Agwunobi. Andy comes to Humana from the University of Connecticut, where he serves as interim University President and as CEO of the UConn Health System. He will join Humana and serve as a member of our management team starting later this month.

He has been responsible for many home health organizations as part of its integrated health systems. He has extensive operational experience with for-profit and nonprofit organizations. And as a doctor, he understands the value of care in the home, why seniors want more of it and our vision at Humana for making it easier for people to get the care they need at home.

Kindred at Home has a strong fee-for-service business that we are committed to continuing to grow. In addition, as I shared last quarter, we have made substantial progress towards our goal of scaling and maturing a risk-bearing, value-based model that manages the provision of home health, durable medical equipment and home infusion services. We believe the model has significant value creation potential, both within Humana as well as payer agnostically.

We have a goal of covering nearly 50% of Humana Medicare managed members under this model within the next 5 years. The home model is active in South Florida and Texas. Today will begin -- and today, we'll begin the rollout of additional markets of Virginia and North Carolina in the second quarter with subsequent rollout to additional geographies this year and early next year. After completing these first 2 phases of expansion, our value-based home health model will provide coverage to approximately 15% of Humana Medicare Advantage members.

In addition to the expansion of the full value-based model, we have the opportunity to accelerate our return on investment by introducing select components of the full value-based home health model, such as stand-alone DME or utilization management services in less dense markets. We believe approximately 60% to 70% of Humana members will be served by the comprehensive value-based model over time while the remaining will be supported by select components based on the needs of the market.

Before I turn it over to Susan, I want to once again emphasize that Humana's core operations are strong, and we continue to create significant value by driving growth in our top-tier Medicare Advantage business, expanding our Medicaid footprint and increasing contribution from our health care service businesses and delivering ongoing cost efficiencies and productivity improvements across the company. Indeed, we have great confidence both in the fundamentals of the Medicare Advantage industry and the long-term growth prospects for Humana.

And as we look ahead, our improved membership growth, combined with further penetration in our growing and maturing health care service businesses, position Humana favorably to deliver on long-term earnings target in 2023 and beyond. We have a proven track record of not only balancing membership and margin to deliver our long-term 11% to 15% earnings growth target but also improving health outcomes and lowering the total cost of care for our members and optimizing our operations through productivity and efficiency initiatives. And we look forward to delivering on our latest targets.

With that, I'll turn the call over to Susan.

Susan Marie Diamond - *Humana Inc. - CFO*

Thank you, Bruce, and good morning, everyone. Today, we reported full year 2021 adjusted earnings per share of $20.64, slightly ahead of our expectations of approximately $20.50.

As Bruce mentioned, despite the challenges we faced in 2021 due to the pandemic, our fundamentals remain strong with the underlying core business delivering solid results for the full year. Including the impact of an unmitigated net COVID headwind of $1, our adjusted EPS grew 11.6% off of our 2020 baseline of $18.50 and our individual Medicare Advantage membership grew 11%, outpacing the industry.

I will now take a few moments to discuss our fourth quarter results and underlying trends before turning to our expectations for 2022. We reported fourth quarter adjusted EPS of $1.24, slightly above internal expectations and consensus estimates. Fourth quarter results for the Retail segment were largely in line with expectations. Total medical costs in our Medicare Advantage business ran approximately 1% below baseline during the fourth quarter, in line with the forecast we shared in early November.

While COVID utilization remained higher than initially expected due to the Omicron variant surge, we continued to see a corresponding reduction in non-COVID utilization through the end of 2021. And this trend has continued into early 2022. Although a smaller percentage of individuals that are infected with the Omicron variant require hospitalization as compared to previous surges, COVID admissions in recent weeks have been consistent with levels experienced in January 2021 due to the significantly higher rate of transmissibility of the Omicron variant. With respect to the flu, trends remained favorable to expectations in the fourth quarter and have continued this pattern in the first few weeks of 2022.

In our Group and Specialty segment, our results were slightly better than previous expectations for both our group medical and our specialty businesses. All-in utilization in our fully insured group medical business continued to run a bit above baseline but slightly better than our previous expectations. Our specialty business results also outperformed as utilization, particularly for dental services, continued to run lower than anticipated. Finally, each of our Healthcare Services businesses performed consistent with expectations in the fourth quarter.

The integration of Kindred at Home operations remains on track. And results post acquisition have emerged as anticipated. Fourth quarter 2021 home health admissions were up slightly while hospice experienced a low single-digit decline as compared to the fourth quarter of 2020. From a full year perspective, we have seen home health admissions up low single digits with hospice admissions down low single digits year-over-year. It is important to note that hospice volumes have been impacted by the higher mortality rates driven by COVID as well as lower post-acute facility volumes.

As I shared last quarter, we are closely monitoring admission and clinical staffing trends and are making targeted investments to sustainably improve the recruitment and retention of nurses to position the businesses for further growth as trends begin to normalize. We improved home health and hospice nurse retention by double digits in 2021, positively growing net nurse headcount in the second half of the year. We also reduced the number of nurses who attrit in the first 90 days of employment in the second half of 2021 for the first time since the pandemic began. While we are pleased with this progress, we acknowledge that the labor market remains challenging, and there is more work to be done to further improve nurse satisfaction and retention.

In our primary care organization, patient growth in our de novo centers exceeded expectations in 2021, increasing 68% year-over-year with these centers now serving over 20,000 patients. We expect this growth to continue into 2022. Finally, our pharmacy operations remained strong with industry-leading mail order penetration. Amongst our individual Medicare Advantage members, 38% of scripts prescribed in 2021 were dispensed by Humana Pharmacy's mail order business, which continues to increase year-over-year.

In addition, in more mature CenterWell clinics, we have seen mail order penetration rates for Humana members approach 50%. And when combined with prescriptions dispensed by co-located Humana retail pharmacies, total Humana Pharmacy market share can approach 60%. Our strong mail order volumes continue to highlight that members value the convenience and cost savings mail order delivery provides, which also leads to better medication adherence and health outcomes benefiting our members and health plan.

Before turning to our 2022 outlook, I would like to add to Bruce's earlier comments regarding our commitment to taking significant actions to create capacity for investments in our Medicare products, which will allow us to significantly improve membership growth in 2023 without impacting earnings growth.

We have already begun taking action to deliver on this commitment, including engaging external consultants to benchmark Humana's operating structure and initiating a deep dive into processes across the organization to ensure that we identify a comprehensive set of opportunities. We are on a continuous journey of improvement and are confident in our ability to remain a leader in the Medicare Advantage industry and deliver on our long-term earnings growth target in 2022 and beyond.

Now turning to our 2022 expectations and related assumptions. Today, we are providing adjusted EPS guidance for 2022 of at least $24, representing growth of 11.6% over our 2021 baseline of $21.50 and 16.3% over our actual 2021 adjusted EPS of $20.64, consistent with our previous commentary. This guidance contemplates an explicit COVID-related headwind of $1 in adjusted EPS.

In addition, as previously shared, we are assuming medical costs return to baseline levels and that costs related to COVID continue to be offset by the depressed non-COVID utilization in our Medicare Advantage business. To the extent the $1 explicit COVID headwind is not ultimately realized, we will be conservative regarding the timing and pace with which we adjust our full year earnings guidance to ensure we do not get ahead of any potential emerging trends.

Our 2022 outlook reflects top line growth above 10% with consolidated revenues projected to be north of $92 billion at the midpoint, driven by continued growth in our Medicare Advantage business and expansion of our payer-agnostic Healthcare Services businesses, partially offset by expected declines in our commercial group medical, Medicaid and Medicare stand-alone Part D or PDP membership. 2022 EPS also reflects the impact of a reduced share count as a result of the $1 billion accelerated share repurchase program entered into in January.

With respect to the forecasting quarterly EPS, we acknowledge it will continue to be challenging, predicting the timing of additional COVID surges and the related rise in COVID costs and offsetting reductions in non-COVID utilization, which generally occurs on a lag. At this time, we expect the percentage of first quarter earnings to be in the high 20s. We will provide updated color on our expected quarterly patterns throughout the year but would encourage investors to focus on the full year results, given these COVID-related timing dynamics.

I will now provide additional color on the 2022 outlook for each of our business segments, starting with Retail. As recently shared, we now anticipate individual Medicare Advantage membership growth of 150,000 to 200,000 members in 2022. We added approximately 138,000 members during the annual election period, including approximately 48,000 D-SNP members. Touching on group MA, we continue to expect membership to be generally flat for 2022 as we do not anticipate any large accounts will be gained or lost as we continue to maintain pricing discipline in a highly competitive market.

From a PDP perspective, we expect a membership decline of approximately 125,000 members for the full year. As previously shared, the overall PDP market continues to decline as more consumers enroll in Medicare Advantage, and we remain focused on creating enterprise value from our PDP plans by driving mail order penetration and conversions to Medicare Advantage. We are projecting approximately 80,000 of our PDP members to convert to a Humana Medicare Advantage plan in 2022.

Finally, we anticipate that our Medicaid membership will decline 50,000 to 100,000 members in 2022. This change reflects membership losses resulting from the start of redetermination, which we expect to begin following the end of the public health emergency in April. These losses will be partially offset by membership additions expected as part of the Ohio contract award, which will go live in July. The addition of the Ohio contract award expands our Medicaid presence to 6 states, which as we have shared before, has been largely accomplished through organic growth.

The Retail segment revenue is expected to be in a range of $81.2 billion to $82.2 billion, reflecting a 10% increase year-over-year at the midpoint. The year-over-year change includes the impact of the normalization of Medicare risk adjustment revenue in 2022, the phaseout of the sequestration relief beginning in the second quarter as well as the impact of changing member mix. The benefit ratio guidance of 86.6% to 87.6% is 80 basis points lower than the 2021 benefit ratio of 87.9% at the midpoint, driven in part by the normalization of Medicare Advantage revenue in 2021, partially offset by the expected return to baseline medical cost trends.

In summary, we are guiding to Retail segment pretax income in the range of $2.35 billion to $2.55 billion for 2022, an increase of 26% over 2021 at the midpoint of the range, which includes the impact of an approximate 50 basis points increase in individual MA margin year-over-year.

Moving to our Group and Specialty segment. We are expecting total commercial medical membership, including both fully insured and ASO products, to decline by 125,000 to 165,000 members. This decline primarily reflects lower small group quoting activity and sales attributable to the COVID-19 pandemic, specifically as it relates to continued actions by our competitors to retain membership as well as the loss of a large group ASO account. These impacts are expected to be partially offset by strong retention of our existing members.

From a profitability perspective, we expect this segment to show nice pretax growth, driven by improved profitability in the group medical business resulting from the rating actions taken to account for the expected impact of COVID in 2022. This improvement was partially offset by a reduction in expected earnings from our specialty business year-over-year as we do not expect the COVID-driven outperformance seen in 2021 to continue. All-in, we are guiding to a pretax range of $185 million to $285 million for the segment.

For our Healthcare Services segment, we expect adjusted EBITDA in the range of $1.675 billion to $1.825 billion for 2022. The 2022 outlook reflects a full year contribution of Kindred at Home and continued growth in our pharmacy and primary care businesses. These items are partially offset by investments to enhance our clinical capabilities and expand our value-based home care model as well as investments to support the continued expansion of our primary care organization.

In our Kindred at Home business, home health admissions are expected to be up mid-single digits with hospice admissions up low single digits year-over-year. As I mentioned previously, Kindred at Home anticipates ongoing staffing challenges in 2022, driven by the labor shortage the industry is currently facing. We are focused on mitigation efforts through targeted investments to improve recruitment and retention of nurses. We expect these investments to continue our second half of 2021 trend of improved retention and net nurse headcount growth providing additional capacity to support top line growth.

In our primary care business, as Bruce shared, we intend to build an additional 26 centers in 2022 under our existing joint venture with Welsh Carson, which when combined with planned acquisitions, is expected to increase our center count by approximately 20% in 2022 and bring our total center count to approximately 250 centers by the end of the year. Patient growth in our de novo centers is expected to exceed 10,000 in 2022, reaching approximately 30,000 by year-end, a 57% increase year-over-year.

From an operating cost ratio perspective, we are guiding to a consolidated adjusted operating cost ratio in the range of 13.2% to 14.2% for 2022, an increase of 160 basis points at the midpoint from the adjusted ratio of 12.1% in 2021. This increase reflects the full year impact of Kindred at Home, which has a significantly higher operating cost ratio than the company's historical consolidated operating cost ratio. The incremental 7.5-month impact of Kindred at Home operations are contributing approximately 150 basis points to the expected year-over-year increase.

I would like to now briefly discuss capital deployment for 2022. We will continue to prioritize investments in our core business to drive organic growth. Strategic tuck-in M&A remains part of our overall framework and we will be prudent and opportunistic as we focus on organic growth in the near term.

And finally, we recognize the importance of returning capital to shareholders. And we expect to maintain our strong track record of repurchases as demonstrated by the $1 billion accelerated repurchase program that we entered into in January. While our debt-to-cap ratio is temporarily impacted by the acquisition of Kindred at Home, we believe we have sufficient capacity to execute on high-priority investments initiatives, such as primary care growth, while continuing to deliver strong shareholder returns.

In closing, I would like to reinforce our commitment to drive $1 billion of additional value for the enterprise through cost savings, productivity initiatives and value acceleration from previous investments in order to create capacity to fund growth and investment in our Medicare Advantage business and further expansion of our Healthcare Services capabilities.

As reflected in our initial guidance for 2022, we have entered the year targeting the low end of our long-term earnings growth range of 11% to 15%, which includes an embedded COVID headwind. To the extent this COVID headwind is not ultimately realized, we will be conservative regarding the timing and pace with which we adjust our full year guidance. We believe entering the year with this headwind incorporated into our guidance is prudent in the current environment. And we are proactively taking steps to position the company to continue to deliver on our long-term targets in 2023 and beyond.

With that, we will open the lines up for your questions. (Operator Instructions) Operator, please introduce the first caller.

QUESTIONS AND ANSWERS

Operator

Our first question comes from Matthew Borsch with BMO Capital Markets.

Matthew Richard Borsch - *BMO Capital Markets Equity Research - Research Analyst*

Maybe if you could talk about how the likelihood of earnings upside for this year, just given the way that you're positioned with a very, I don't know, very -- but a conservative MA bid for 2022. Don't you think that would make margin upside more likely as you move through the year?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. Thank you. So certainly, as we've said repeatedly, we definitely are approaching our 2022 guidance with conservatism, which we think is a prudent thing to do. We've disclosed the explicit $1 COVID headwind, which is embedded in our guide. And while we do consider that conservatism, we do just want to reinforce that there remains to be a lot to learn about COVID. There are certain dynamics that continue to emerge, things like whether Medicare will cover over-the-counter testing. We continue to watch the trends in terms of hospitalizations due to COVID.

As I mentioned, while the Omicron variant seems to be less severe, it is much more transmissible, leading to many more COVID hospitalizations, some of which are not frankly directly related to COVID in terms of the admitting condition, but rather they're being admitted and happen to test positive for COVID. And that results in that extra 20% payment that's provided for under the public health emergency. So those are just two examples of the things that we'll continue to watch, which may prove to be that the $1 COVID headwind becomes necessary.

But as we've said clearly, if it proves that, like we've seen historically, that all of the COVID costs continue to be offset and that proves to be conservatism, then you will see that released over the course of the year through additional earnings. And if the entirety of that $1 was not needed, then we would end up above the high end of our long-term targeted range. But just again, encourage everyone to not get ahead of us on that as there's still a lot to be learned and monitored as it respects to COVID trends over the coming year.

Operator

Our next question comes from Justin Lake with Wolfe Research.

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

A couple of numbers-related questions here. First, on the $1 billion, can you talk about how much of that $1 billion will be cost-cutting versus other value creation? And what's the timing of the benefit here in '22 versus '23 and beyond and whether any of this benefit is assumed in 2022 EPS?

And then quickly, just in your release, you reiterated your 11% to 15% earnings growth target for 2023 and beyond. Should we take that to indicate that you expect to grow 11% to 15% next year despite the headwind of lower membership growth from this year?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. I can take that, Justin. So for your first question about the $1 billion cost-cutting, how much is cost-cutting, Bruce laid out four sort of high-level categories that we expect to contribute to that overall goal of $1 billion in value creation. We would estimate currently that each of those will probably proportionately contribute to that goal evenly over those four categories. There's still a lot to be done to finalize discrete initiatives and the timing of those. But that is our initial thinking. And we'll certainly keep everyone apprised of our progress towards that goal as we go through the year and finalize some of our 2023 pricing and bids.

As it respects to the timing of that, as I said, we continue to work on the detailed assessment of opportunities that will lead to a variety of implementations over the course of the year. We are highly motivated to create a path to that. So we have a run rate going into 2023, so we can count on that in pricing. And we would certainly expect some benefit from these actions in 2022, although the benefit would be meaningfully smaller than our overall 2023 target, expecting that most of these initiatives would be implemented late in the year and so contribute less obviously to 2022 guidance.

As we discussed recently with the reduction of our 2022 individual MA membership growth expectations that, all other things being equal, would have some negative impact to 2022. Certainly, any acceleration we can get from the $1 billion value creation activities can certainly help as one of the puts and takes that we always consider as we finalize our full year forecast. So all-in, again while we might have some impact from these initiatives and acceleration, that would be contemplated in our guide. And it's just one of many things that we consider as we go out with our initial guidance.

As it respects to 2023 and beyond in our commentary, we do remain committed to delivering against our long-term earnings growth target. We believe that the actions we'll be taking this year to position us to return to leading growth will help us do that without negatively impacting our expected long-term EPS target. So that's our current expectation. And certainly, we'll continue to keep you apprised as we go through the year.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

And Justin, just to maybe create some clarity on when we talk about the initiatives that we're focused on, on slowing down, I just want to reemphasize to the shareholders that we are very oriented to growing the primary care in the home area. And so those initiatives really would continue to see the planned investments in those areas. There's other areas that we will slowly grow or pause as a result of this $1 billion goal.

Operator

Our next question comes from Kevin Fischbeck with Bank of America.

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

I guess, maybe just to go into this $1 billion value comment a little bit more, I mean, some of these sound like things that as an enterprise you would be doing to some degree every year anyway. I mean, how should we think about this $1 billion number? Is it incremental to what you would normally be assuming? Or is it -- and you normally get $300 million and now you're doing $1 billion. And it sounds like, I just want to confirm, that this is separate and distinct from trend benders, but just wasn't sure if trend benders were part of this $1 billion.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes, I'll take that. It is in addition to what we normally have seen over the years. As you know, we've continued to focus on our productivity. We do believe a number of investments that we've made over the last few years are ripe to really help with the productivity side of our organization. And in addition, I think there's some number of them that will also provide some clinical and additional clinical benefits for us. So this is in addition to our normal, as you referred to the trend benders, our clinical outcomes there. So we think about the investments there.

But to be frank with you, we are pushing the organization to be more efficient. This is a much more larger effort for us as an organization. We feel that we have significant opportunity to do it. We believe that focusing on investing in our customer is the top priority for us and continuing to expand the Healthcare Services side. So that just takes a continued refinement of where we spend our money and focus on continuing to be more efficient.

Operator

Our next question comes from Stephen Baxter with Wells Fargo.

Stephen C. Baxter - *Wells Fargo Securities, LLC, Research Division - Senior Equity Analyst*

I wanted to ask another one about the $1 billion. Any rough sense you can give us on how much of that will be allocated to Medicare Advantage versus Healthcare Services? And then within Medicare Advantage, how should we think about the balance between benefit improvement and what you're talking about doing on the marketing side?

And I guess, the continuation of that question would be should we think about the entirety of that benefit as accruing to 2023? Or is there then going to be an incremental benefit from some of these efforts as we move into 2024? Just trying to think about how the growth acceleration could be sustained as we move past 2023.

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. Stephen, I'll take that. So the value creation will span all segments. Different segments that will probably contribute a little bit differently. Certainly, in our MA business and the scale at which we operate, as Bruce mentioned, we might expect more efficiency opportunities in that business versus within Healthcare Services, where we're still looking to grow particularly in primary care, where it's less mature, and then within Kindred, as we described, focusing on improving nurse retention for the purposes of creating additional capacity to drive top line growth is where we might focus.

So it will look a little bit different. I would say, in places like Healthcare Services, we'll look for opportunities to optimize the business performance to improve additional pretax contribution and value acceleration, where some of our more mature businesses will likely see more benefiting from more traditional cost initiatives and productivity.

In terms of how we'll use the capacity that we create, that will be a combination of benefits, marketing and distribution on the Medicare side as well as continued investment in Healthcare Services across pharmacy, primary care and Kindred in order to support some of our forward-looking capabilities there. So how exactly that will be allocated will be determined based on some additional work that still needs to be done as we approach our 2023 bids.

Our teams are actively working to assess the impacts of the 2023 selling season and formulate their recommendations in terms of how to best optimize those investment dollars across product, marketing and distribution. It's hard to say right now whether we can fully get back to industry-leading growth by 2023. That certainly would be our goal, and we'll work hard to see if we can do that.

But recognizing the rate notice still needs to be reviewed once that comes out and a variety of other factors we'll need to consider, that will ultimately determine whether we can do that in 1 year or whether it takes a little bit longer. And again, as we go through the year, we'll keep you apprised of our efforts. But certainly, we'll work hard to accelerate growth as quickly as possible.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

On your question on '24 and if it's sustainable, our objective in this $1 billion goal is to have a significant amount of the savings to have a sustainable year-by-year. This isn't just a 1-year shot. We're looking to really focus on the improved productivity as an important part of that. Obviously, the clinical programs we can build off of are really two areas that we look at as having sustainable long-term impact.

Operator

Our next question comes from A.J. Rice with Credit Suisse.

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

I think I might just ask you about the primary care centers. It's been a while since you talked about the economics of those. I know, Bruce, in your comments, you said that a maturity -- a center could contribute $2 million to $4 million. Can you talk a little bit about how long it takes?

Any updated thoughts on how long it takes to get to profitability? And then once you get to breakeven, how long it takes you to get to that mature margin? And on a center, what would a $2 million to $4 million represent in terms of an EBITDA margin? Maybe just flesh that out a little more.

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. So I think as we disclosed before, we anticipate that it will take roughly 3 to 5 years to deliver and achieve mature operating performance within an individual de novo clinic. And we, through our Welsh Carson partnership, seem to be on track to deliver that.

I don't believe we've disclosed the targeted margin for our primary care centers. But I think what we've said previously, we don't believe that our operating performance would look meaningfully different than others that are operating in the public space, other high-quality performing providers. So we have every reason to believe that our cost will be similar to others and performance level.

Operator

Our next question comes from Josh Raskin with Nephron Research.

Joshua Richard Raskin - *Nephron Research LLC - Research Analyst*

I want to get back to the $1 billion in additional value and specifically the impact on Humana. Is all of that getting reinvested to help longer-term growth? Or does some of that actually -- some of those savings actually fall to the bottom line?

And then you talked about areas where you have the greatest conviction on significant value potential. Should we assume that, that means primary care in the home? I apologize for the run-on question, but the last part would be, you've spoken about a 4.5% to 5% target MA margin for the individual MA. As you put this together in terms of this value creation project, is there a different thought on target margins? And is that -- should we be thinking more about enterprise-level margins as opposed to individual MA?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. Josh, I can take that. So in terms of your first question about whether the $1 billion investment would fall to the bottom line or be reinvested, I think our thinking right now is that it's likely to be predominantly reinvested into high-priority areas, including Medicare product, distribution and sales as well as primary care in the home.

Having said that though, that allows us to return to industry-leading growth. Just the trajectory of that membership growth and the resulting benefits to the full enterprise and the variety of capabilities and services that support those members, that can also allow for some of that margin expansion over time as well.

In terms of the references we made to value creation, what that's recognizing is that over the last number of years, we've made meaningful investment in a variety of areas, things like consumer experience, technology platforms, digital and analytic capabilities as well as on the Healthcare Services side within primary care in the home as well as pharmacy.

And what we're going to ask the enterprise to do is rather than embark on additional investment in some of those capabilities, rather focus all of our resources on maximizing value creation out of those investments we've already made. And we believe that, that will lead to opportunities to accelerate value creation for the enterprise that can then be reinvested into all of those things I just mentioned.

And one example of that is the introduction of our value-based home health model. While we envision a comprehensive model that Bruce described in his remarks, there are also opportunities to deploy discrete elements of that, whether that's stand-alone DME or utilization management in markets that maybe don't have the density to support the full model and that we can accelerate some of that to generate additional value for the enterprise. So those are things that we'll ask the team to focus on and just maximize return off the investments we've made to date rather than continue to invest incrementally more in the current time frame.

On the margin question, so again we remain committed to our long-term individual MA margin. We're pleased to announce that we'll see some progress, positive progress this year as we mentioned in my remarks. We expect expansion of about 50 basis points in 2022. We think that, again over time, as we return to an industry-leading position and scale some of our other businesses, that does allow us to continue to expand margin long term discretely within the health plan.

But also, as we've said before, we think it is important that everyone continue to focus on the broader enterprise margin potential off of our health care services capabilities, which as we continue to expand the coverage of primary care in the home and increased penetration in pharmacy, those discrete contributions allow us to add significantly more value to the enterprise off of that base in individual MA membership long term, such that we should be able to see even greater enterprise margin expansion over time. And as we continue to grow those businesses, that will just become an increasingly important part of our value creation story and support our long-term sustainable EPS growth target.

Operator

Our next question comes from Scott Fidel with Stephens.

Scott J. Fidel - *Stephens Inc., Research Division - MD & Analyst*

Two just quick numbers questions, if I could. The first is just if you could update us for the MRA headwind related to the pandemic, where that ultimately came in for 2021? And then it sounds like are you assuming that you're going to fully normalize on the risk scores in 2022? Or maybe if you could just talk to specifically how much improvement you expect on that.

And then just a second one, if I could. Just as it relates to HH&H and as we think about what you had previously told us you're planning to do with hospice, I remember that when you had initially gave us the presentation on the acquisition, there was a 50-50 split that you talked about between home health EBITDA versus hospice EBITDA. Still just interested if that's where it's tracking heading into 2022 as well.

Susan Marie Diamond - *Humana Inc. - CFO*

Great. Thanks, Scott. So for the first question related to premium, so yes, we gave disclosures throughout 2021 as we continue to track the submission of diagnosis codes, which obviously was important into returning to more normalized premium levels for 2022. So we did continue to see diagnosis code submissions track as we expected. It's important to consider that the January premium overall is also going to reflect the impact of members newly enrolled or disenrolled.

It also now reflects the impact of the higher mortality that we experienced as a result of COVID. We've mentioned that we've been studying those impacts for some time, recognizing that the members who passed away as a result of COVID had higher-than-average risk scores as well as higher-than-average claims, recognizing that individuals with multiple chronic conditions were the most susceptible to severe COVID complications.

So you will certainly see that reflected in our premium yield for the year, which all other things being equal, will be a little bit lower than we otherwise would have expected because of that higher mortality due to COVID. Again, the claims also run higher for that population and the results of both of those dynamics are reflected in our estimates. So we do expect our individual MA PMPM yield to be in the high single-digit range for 2022.

Scott J. Fidel - *Stephens Inc., Research Division - MD & Analyst*

And then Susan, just on the HH&H EBITDA?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. And then yes, on your question, yes, as you mentioned, when we disclosed the transaction, it was roughly 50-50 split. Hospice had slightly higher margins than the home health business. And those trends continue. So that's a reasonable assumption.

Operator

Our next question comes from Kevin Caliendo with UBS.

Kevin Caliendo - *UBS Investment Bank, Research Division - Equity Research Analyst of Healthcare IT and Distribution*

So I wanted to just talk about the third -- you talked about extra training for third-party sales. And I just want to get to the bottom of this whole disclosure situation. Do you expect the market to sort of move in your direction? Or can you talk a little bit about how you're going to change or what exactly the training might be to sort of fix the messaging in that channel?

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes. Let me start and I'll look to Susan to add. We'll continue to work with our external partners on being able to ensure that our customers and frankly the industry customers are properly -- have the proper understanding of what they're buying. At the end of the day, that's what we're trying to ensure on. Our disclosures are not much different than others in the marketplace. And the time that people spend on our members and throughout the industry, I think, are about the same.

But we do believe, considering just the sales channel itself continuing to reemphasize to our -- to the members, Medicare members in totality and understanding what they're buying is very important. We are seeing increasing interest by CMS around this particular matter. And in fact, you saw it in some of the regulations that came out in the early part of January that they continue to be oriented to this particular area here.

Operator

Our next question comes from Ben Flox with Jefferies.

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

Is that Dave Windley that you were trying to -- is it me? So Dave Windley here, sorry for the confusion on that. But my question would be how synergistic, Bruce, are your primary care in the home, your home health initiatives and your primary care clinic initiatives? And to what extent -- I've noticed in some of your releases, some of the same states. But to what extent are you focusing your efforts in those two areas on the same local markets to drive kind of duplicative impact?

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes. That's great question, David. We actually refer to that internally as the flywheel and the ability for us to leverage the touch points with our members in the various different providers. And that would also include the pharmacy side. And we're seeing great benefit from that all the way from obviously driving more volume, better clinical outcomes as a result of the coordination that's there and then, in addition, driving higher satisfaction. So it's really touching all parts.

What I would say is what you see, we started -- primary care is much more focused in the markets they're in, while Kindred has a much broader platform that can be wrapped around the primary care side. And so in a few markets this year, we're actually going to work on the integration of that together. And that's one of the reasons why you also see a consistent brand around CenterWell, where we're beginning to start to integrate that.

So I would say 2022 is a year of beginning that process. But I would say subsequent to 2022, you'll see a lot more activity in the local market of much more integration around the care model. And in addition, we see significant benefit from that.

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

Is it too -- if I could ask, is it too early to know numbers of like how much you bend to trend or cost savings from that flywheel? Do you have any...

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes. We usually see between 2 to 4x better outcomes, when I say that, both financially and clinically as a result of the ability to bring this in.

Operator

Our next question comes from Ricky Goldwasser with Morgan Stanley.

Rivka Regina Goldwasser - *Morgan Stanley, Research Division - MD*

Staying on the primary care, 206 centers now expanding throughout the year. What percent of Humana's MA members overlap with your primary care centers? And what type of retention rate you see with these members versus the rest of the group? And then secondly, just to clarify, we talked about the $1 billion in value creation. But as you think about that value creation, how much should we assume is going to come from gross cost-cutting initiatives?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. Ricky, so on the first question, I'd actually have to get back to you on the actual technical coverage in terms of our CenterWell clinics overlaid to our Medicare memberships. So we can get back to you with that number. I don't believe we've ever disclosed anything specific to retention related to Humana members in those clinics.

I will just point out that our clinics do provide care agnostically. So they have many other health plans that they serve. And so even if a Humana member should choose to enroll in another plan, they have an opportunity to preserve that member, should they participate in those networks as well.

As those centers continue to expand, that is an area that we are very focused on and really understanding sort of the experience that they're providing to patients and working to ensure that those -- that they have industry-leading retention within those clinics as well. And they do have very high NPS and patient satisfaction as a result of the high quality and comprehensive care that they provide.

On the $1 billion of value creation, as I mentioned, the four categories that Bruce described, we think, will contribute roughly equally to our overall goal. And so as he described, there are -- there is a component that is related to value acceleration, which we think can impact a variety of top line growth opportunities or trend savings, et cetera.

But the other categories do involve really taking cost out of the system by working more efficiently and effectively, eliminating sort of lower-value work as a way to get more streamlined and focus our associates on the most important work in front of us.

Rivka Regina Goldwasser - *Morgan Stanley, Research Division - MD*

So should we just interpret it that you said equally? So do we just take the $1 billion and saying $250 million in gross cost savings? Just trying to think about how should we flow that through the P&L.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. So as you think about the -- Bruce laid out four categories. There's the supply chain, which again that is savings as well. So I'd say, really it's more like 3/4 of the total is probably going to come from various savings initiatives and then about 1/4 from other value acceleration opportunities.

Operator

Our next question comes from Whit Mayo with SVB Leerink.

Benjamin Whitman Mayo - *SVB Leerink LLC, Research Division - MD of Equity Research & Senior Research Analyst*

I wanted to go back to Kevin's question on third-party marketing for a second, maybe just ask this a different way. I think there's still some confusion. When CMS issued their October memo last year around compliance and your oversight of first tier and third marketing organizations, did you pull back materials in the market? Did the actual compliance requirements have an impact on you? I'm just trying to understand if you were out of the market and if you think you have a better view on how to course correct this.

Joseph C. Ventura - *Humana Inc. - Chief Legal Officer*

This is Joe Ventura. I'll maybe handle that one. We've done a variety of channel checks with our partners to make sure that we were not an outlier when you look at the compliance requirements that came out of CMS. I think as you all know, it was a recognition of responsibility for third-party marketing on behalf of all of the payers.

And so our channel checks confirm that we were not an outlier. Our partners are working in this way with other large payers as well. As Bruce mentioned, to make sure that our members, when they call and they purchase a plan, they know what they are purchasing and that they're aware and that it's a good quality sale for them.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Just -- I know there's a lot of interest in this, so maybe just to provide a little more clarity here. What we find in this channel is there is a high degree of confusion that is with the members and what they buy. That's one of the reasons why you see the high churn. And it has created a number of downstream issues, both the confused and -- members and then in addition, just some compliance issues. And that's why you see the efforts by us and other organizations to ensure that we ensure that the individual is properly purchasing the plan that they choose.

Operator

Our next question comes from Nathan Rich with Goldman Sachs.

Nathan Allen Rich - *Goldman Sachs Group, Inc., Research Division - Research Analyst*

Thanks for the question. Maybe just trying to pull together the commentary on the value creation program, I guess, do you envision it allowing you to return to market growth in individual MA kind of while maintaining the target margins that you have for that business by leveraging those savings?

And I guess, the follow-on to that would be the $1 billion would give you over 100 basis points of margin to kind of reinvest in that business. Can you maybe talk about where those investments would be focused? And then a quick follow-up, if I could, with the '23 rate notice coming imminently, do you have any expectations that you can share? And how significant of a swing factor do you feel that is for next year, given that you are making kind of significant organic investments in the MA product for '23?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. So as it respects to value creation goal that we've set, that is with the intent of allowing us to invest in the Medicare business as well as Healthcare Services and return to industry-leading growth not at the expense of margin. So the intent is that, that will be reinvested such that we don't deteriorate margins but rather maintain and then over time, continue to expand MA margins toward our long-term goal. And we believe that, that target savings and value creation opportunity will allow us to do that.

In terms of where we'll focus those investments, I think within the Medicare business, as I said, there's a lot of additional work to be done. But certainly, we will make product investments. As we analyze our results in the D-SNP space, while we continue to grow nicely, we're not growing as much as we had last year. And there are certainly opportunities to enhance that product offering that we think will allow us to get back to a leading position in D-SNP. And we'll look at other opportunities by product as well as geographically to do that and be really thoughtful in the way we optimize any investments that we're going to make.

We also are looking at distribution as we've been discussing and what opportunities there may be there in terms of further investment in incentives to encourage retention and other things, to optimize those channels as well as marketing. We'll continue to look for ways to increase our share of voice, as Bruce described, but also ensure we're getting the highest return on that investment. And there's likely some opportunities to do more there.

In terms of the rate notice, we're as anxious as everyone to see that. That should come out soon. Based on the strong bipartisan support of the program and the strong enrollment and continued enrollment by Medicare beneficiaries as they choose MA, given the value that it provides to consumers, we would expect that, that would be more moderate. Our expectation is that it may not be quite as favorable as we've seen in recent years, but our expectation is not that it's negative either.

But certainly, this is -- we recognize that it's the first rate notice. We'll see how the Biden administration and look forward to seeing that and hope that it continues to support the program and all the beneficiaries that it serves.

Operator

Our next question comes from Gary Taylor with Cowen.

Gary Paul Taylor - *Cowen and Company, LLC, Research Division - MD of Health Care Facilities and Managed Care*

I just want to ask a little bit about value-based care, CenterWell. Conviva noted your announcement about the center expansion and expectations for continued tuck-ins. It does look like at least there's a modest increased investment that you're making there for all the reasons that you've highlighted historically. What I want to ask about was what is your appetite to do something beyond just tuck-in?

I think you said last year, 15 centers acquired at 9 different transactions. We've seen in the public market an enormous valuation correction, which presumably ultimately flows through the private market as well. And we know there's a number of private companies with much larger center counts that have pretty significant overlap with your MA penetration. So just wondering if there's an appetite on the tuck-in side to do something larger in an environment where valuations seem more reasonable.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Gary, just a few things. On the tuck-in ones, we see those as just great opportunities because we can buy them at a fairly low multiple as a result of the synergies that we get in the marketplace there. So they are very -- they're great deals for us overall. So we want to continue to do those. And as you have seen over the years, we have been very sensitive to how we utilize our capital and sensitive to valuations because we do believe over time, the ability to drive value, we see greater in the organic side and just densifications in the markets that we're in.

That being said, I mean, we would -- we obviously would look at those companies there. We still think the valuations, albeit they've come down quite a bit, we continue to look at them and say, "Are they at a level that would make sense today?" I just question a little bit of that. But that being said, we would continue to look at them. But I just -- we just feel what we're doing in the organic side, combined with tuck-ins, is really driving -- will drive significant amount of value for the shareholders over a longer period of time and can continue to advance our strategic positioning.

Operator

Our next question comes from Lisa Gill with JPMorgan.

Lisa Christine Gill - *JPMorgan Chase & Co, Research Division - MD, Head of U.S. Healthcare Technology & Distribution Equity Research and Senior Research Analyst*

I want to go back, Susan, to your comments on the PBM side of the business. You talked about Rx being up 8%. What's your expectations going into 2022 around script growth? And then secondly, what are some of the opportunities you see when we think about specialty and biosimilars for your PBM for 2022?

Susan Marie Diamond - *Humana Inc. - CFO*

So with respect to the pharmacy business, as we look at our 2022 expectation, certainly with the lower-than-expected MA growth, that will have some impact to the PBM year-over-year. But we also had outperformance in the stand-alone Part D space, which to some degree offset, although our PDP members don't use mail quite the same rate as our individual MA, so a little bit of a negative relative to what we would have expected. But otherwise, we'll continue to work to drive mail order penetration. And then certainly utilization trends are expected to continue to increase as you would expect and consistent with historical trends.

On the specialty side, the team does continue to look at opportunities in the specialty space and evaluate ways to both provide services agnostically but also continue to drive their ability to participate in distribution of various specialty-related drugs. So they continue to look for ways to expand that business. The other thing that they do is they work very closely with our health plans. What we like about our own specialty business is they are really working towards the health plan goals, which is to reduce waste and ensure that we're reducing the cost of those high-cost specialty drugs where and when possible. And we think that's a real advantage to having our own specialty pharmacy, which is very focused and oriented to the health plan goals.

Lisa Christine Gill - *JPMorgan Chase & Co, Research Division - MD, Head of U.S. Healthcare Technology & Distribution Equity Research and Senior Research Analyst*

And when I was asking about biosimilars, I think I'm thinking specifically to something like Humira that will lose patent protection in 2023. Is that -- it's a delivered product to the home. Is this something that will be beneficial to Humana?

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

It could be. I mean, again as what we've seen as they enter generic status, it is a great opportunity for the PBM to drive value. What ultimately happens is we do drive those rebates back to our customer and lower the Part D costs. So as you think about just the opportunity here, it's always around how do you create a competitive product in the marketplace. But it is an opportunity for us.

Operator

Our next question comes from George Hill with Deutsche Bank.

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

Bruce and Susan, I want to give you a chance to kind of clarify something on the $1 billion in value creation, given the questions that I've already gotten this morning, which, I guess, is can you talk about how much of the $1 billion we should think about as cost savings or initiatives that flow to the bottom line versus initiatives that are taken to accelerate revenue growth or growth in the services segment?

And then my follow-up to that would be can you talk about the incremental spend that will be required to achieve the $1 billion kind of above and beyond what was previously planned? Just I'm getting this -- some analysts and investors are already reading that $1 billion through to $1 billion and operating line savings, which I don't think seems to be the case.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes. Let me try to clarify that. I think our intention is really to reinvest it in the customer value to be -- I think ultimately, it will show back up in the bottom line through higher growth. And as you all know, right, we all are focused on how do we continue to grow our customer line. And we feel today we have the opportunity to find -- to invest in both the channel, the marketing and, in addition, the product itself to drive that value. So from an investor's point of view, I would look at more of the top line benefit from comes from that than the bottom line, just the margin itself. So it's a much harder math to do, but it is something that's very oriented to top line growth.

In regards to just the structure of the cost savings of it, as we've talked about on a few occasions, it is a combination of cost savings, taking costs out of the system, being both efficient and eliminating things that are at lower value and, at the same time, improving revenue but mostly clinical cost as a result of it. So there will be -- when you think about the income statement line item primarily, it will show up in the operating expenses with a little bit showing up in the area of the administrative -- on the clinical piece.

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

That's helpful. Maybe anything on the incremental spend?

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Incremental, that's a net number. As we look at that $1 billion, it is a net number for us.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. The only thing, George, as we acknowledged in the release is there may be one-time charges related to some things that we do like real estate, getting out of certain real estate. And so those, we would intend to non-GAAP related to any one-time charges in order to realize some of those run rate savings.

Operator

Our next question comes from Rob Cottrell with Cleveland Research.

Robert Sohngen Cottrell - *Cleveland Research Company - Research Associate*

Just quickly, curious if you can comment on your expectation for additional individual membership, individual MA lives throughout the course of 2022, given you're already 80% of the way towards your full year guidance? And then within that, I think, Susan, you commented that you expected to convert 80,000 PDP members to MA in 2022. How many of those have already been converted as of January?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. Thanks, Rob. On individual MA growth, we continue to monitor our trends both sales in terms into the open enrollment period that runs through March. And I would say that generally speaking, those trends continue to track consistent with our full year guide -- adjusted full year guide. So we continue to feel good about that.

On the PDP, I would say the seasonality of the PDP looks similar to overall sort of growth seasonality, where you do see a disproportionate amount in January. But we do have an opportunity in PDP conversions in particular with low-income members, who do have the opportunity to move throughout the year. So it's not quite as weighted to January as overall growth but still more than 50% certainly is realized in the month of January.

Operator

Our next question comes from Steven Valiquette with Barclays.

Steven James Valiquette - *Barclays Bank PLC, Research Division - Research Analyst*

So I think you touched on this maybe a little bit, but just wanted to come back on the topic of commissions into the individual MA market. I guess, if we go back 2 years ago, my sense was that Humana and other major carriers were more than happy to pay full commissions in all distribution channels and would actually be willing to pay more if not for the regulated caps on the commissions. But obviously, in some of your commentary from early January, it sounded as if Humana was perhaps not paying maximum commissions in certain channels.

So really a couple of questions around that. I guess, with hindsight, do you think you were alone among major carriers on not paying maximum commissions, particularly in the telephonic channel that is kind of at the epicenter of all the recent discussion? And also with better hindsight, with a little more passage of time, how big of a role did this particular variable ultimately play in the somewhat disappointing AEP? And then just remind us on your commission strategy around that going forward from here, just to kind of round out this part of the conversation.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Yes. Let me start here. I think, first, just to remind the investors, actually we will be close on our sales this year. So it was more of a retention issue as opposed to sales issues. So I just want to put that in some context as we think about commissions.

We, today, pay the market value, the maximum commission on the sale itself according to the regulations that are out there. There are a number of other dollars that are invested in the external channel, the telephonic channel. That includes marketing, includes some additional incentives that are more oriented to the company as opposed to the salesperson itself. How the company distributes those and does that, we really don't get into -- involved in that.

So when we talk about the commissions in total, we talk about there's different levels that are invested with the partner. We have been more reserved in where we spend those dollars just because we also find there are more effective ways to do that in other channels over the past number of years. And when you look at our sales success, even this year, you see that the commission side is an area there. But it does motivate churn in the marketplace. That's really what we are communicating to.

And that does hurt us this year. And I would say so as others sort of ramped up the payments, too, it did hurt us on the churn side as opposed to the sales side. Going forward, I don't think we're going to provide that kind of detail today. Obviously, it's early, but it's also a competitive market out there. And we want to make sure when we do something, that it is done more proprietary in the way we approach it.

Operator

That concludes today's question-and-answer session. I'd like to turn the call back to Bruce Broussard for closing remarks.

Bruce Dale Broussard - *Humana Inc. - President, CEO & Director*

Well, thank you, and thank you for your continued interest in the company and investing the time today. I hope our comments were put that Humana is in a great position. I think we will continue to lead the industry both in the ability to drive membership growth and, at the same time, improve the health outcomes for the people we serve. And obviously, I want to thank our 90,000 associates and teammates that make this happen every day. Because without their work, we would not be as successful as we are. So thank you. And again, thank you for your support.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.

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