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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good day and thank you for standing by. Welcome to Humana's Fourth Quarter 2023 Earnings Call. (Operator Instructions) Please be advised that today's conference is being recorded. I would now like to hand the conference over to your host today, Lisa Stoner, Vice President of Investor Relations. Please go ahead.

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

Thank you, and good morning. I hope everyone had a chance to review our press release and prepared remarks this morning, both of which are available on our website. We will begin today with brief remarks from Bruce Broussard, Humana's President and Chief Executive Officer; and Jim Rechtin, Humana's President and Chief Operating Officer.

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 2023 earnings press release as they relate to forward-looking statements, along with other risks discussed in our SEC filings. We undertake no obligation to publicly address or update any forward-looking statements in future filings or communications regarding our business or 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 financial press release. Any references to earnings per share or EPS made during this conference call refer to diluted earnings per common share. Finally, 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. With that, I'll turn the call over to Bruce Broussard.

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

Thank you, Lisa, and good morning, everyone, and thank you for joining us. We're going to dedicate the majority of our time today to Q&A, but I wanted to first highlight a few key messages that we hope you'll take away from our discussion today.

As shared in our prepared remarks, which we posted this morning along with our earnings release, I'd like to start by stating the obvious. We are disappointed in the update provided today. The Medicare Advantage sector is navigating a complex and dynamic period of change as we are all working through significant regulatory changes while also absorbing unprecedented increases in medical cost trends. The increase in utilization that emerged late in the fourth quarter was a significant deviation from an already elevated level impacting the industry. We take our commitments seriously and are disappointed, where we are unable to fully offset these higher cost trends despite our best efforts to identify mitigation opportunities throughout the year.

While the near-term impacts of the higher utilization are disappointing, our confidence in the long-term attractiveness of this sector and our position within has not changed. We provided you with our initial outlook for 2024 of approximately $16 in adjusted EPS. Given the recency and magnitude of the uptick in the utilization trend, we have prudently assumed that the higher costs seen in the fourth quarter persist throughout 2024. Based on our review of our initial claims data, we believe that the seasonal factors are not driving the increase. We are committed to updating you on our progress and understanding and addressing this change throughout the year.

Importantly, the MA program was designed to be dynamic and respond to changes in medical trends. Looking to 2025, we are evaluating MA pricing actions and expect earnings growth in other lines of business as well as our ongoing productivity and trend-mitigation initiatives to quickly restore our margins and resume a path of compelling earnings growth. Our current expectation is to deliver $6 to $10 of adjusted EPS growth in 2025. Notably, any outperformance we achieve in 2024 will be additive to this initial outlook.

Before turning to Q&A, I'd like to provide Jim Rechtin, our President and COO, an opportunity to provide a few comments on our update this morning. Jim?

James A. Rechtin - *Humana Inc. - President & COO*

Thanks, Bruce. I am stepping into this role here at Humana at a time that is clearly challenging, both for Humana and for the industry. Despite those challenges, it's been a very positive first few weeks. I've had the opportunity to work with a team that's quite focused, that has clarity of thought and objectives, and no shortage of effort trying to address these challenges. Despite the pressures we're facing right now, I remain as optimistic about this opportunity today as I was 3 months ago when I agreed to step into this role. It's early in my tenure, but I do want to share just a few thoughts with the investment community.

I have been impressed by the leadership demonstrated by this team. There's a clear sense of urgency in responding to the utilization trends impacting the industry. The entire management team has been working tirelessly to understand the underlying issues that we've discussed today, and I'm confident in the approach that the team has taken with respect to assumptions around the utilization pressures we are facing. I also share the conviction of the rest of the management team regarding the need to prioritize margin recovery in 2025 and the significant multiyear opportunity that is in front of us.

We operate in one of the fastest-growing sectors in health care. Humana is uniquely positioned to bring significant value to our members, and I'm confident in our ability to drive long-term value for the health care system and for our shareholders. I look forward to meeting many of the participants on this call over the coming months, as well as many of our talented employees and associates across the organization. Thanks.

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

Thank you, Jim. We will now turn to our question-and-answer session, where Bruce will be joined by Susan Diamond, our Chief Financial Officer. (Operator Instructions). Operator, please introduce the first caller.

QUESTIONS AND ANSWERS

Operator

Our first question comes from the line of Kevin Fischbeck with Bank of America.

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

All right. Great. I guess I wanted to understand the thought process around the 2025 EPS improvement. It sounds like from Jim's comments that you're going to be prioritizing margin that year. Do you think that your -- that this is an industry problem and therefore, the industry will be prioritizing margins similarly so that you will actually be growing in '25? Or is this a view that you're going to be growing below average in '25 to get to that?

And because you're talking about feeling confident about the business, should we be thinking about similar growth in '26 and '27 so you get to that $37 EPS number maybe on a 2-year lag? Is that the right way of thinking about it? Or is there a reason to believe that, that margin target you had for $37 is no longer the right margin target in the medium term?

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

Kevin, why don't I take the industry side, and then I'll turn to Susan on the margin question you had. Because I look at next year as a year that I think the whole industry will possibly reprice. I don't know how the industry can take this kind of increase in utilization, along with regulatory changes that will continue to persist in 2025 and 2026. And therefore, I look to the industry to have disciplined pricing as a result of this.

Obviously, for us as an organization over the last few years, we have tried to maintain that discipline. You can see that in just our rankings and in pricing, we've usually been in the third to fourth ranking. And so we've tried to maintain that. But I do believe the industry will need to price appropriately.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. And Kevin, as we thought about the commitment for 2025, certainly, there are inherent dependencies within that. One is the rate notice, which we obviously don't have visibility into. And so that will be one significant input. Which is why we felt the need to give a wider range at this stage.

The other big dependency is going to be, just as you said, the level of competitor action and need to take pricing as well. And so that, we will continue to watch peer commentary in terms of their results and signals that they send, but that is something that we will have to consider based on the pricing action we ultimately take, of what impact might that have to near-term membership growth.

As we've said a couple of times over the course of the year, we do intend to be very targeted in some of our pricing actions. There are some plans and geographies that are seeing more underperformance than others. And so you may see disproportionate impact in those areas as to both the recovery, but then also the membership, which we feel are no-regret moves to make sure that the financial performance is as we would expect.

So '25 may be a repositioning year where we may see lower than industry average growth depending on the level of competitor pricing actions, but we would feel that we would be repositioning for sustainable growth on a go-forward basis in terms of membership at a more sustainable margin over the long term.

As -- in respect to '26 and '27, obviously, we can't comment on that at this point. We wanted to be clear, given the significance of the impact of '24, what you can expect for '25. We've committed to coming out later this year once we have a benefit of going through all of our pricing work and providing you with an update on that as well as certainly, we'll keep you informed of the emerging trends. But we'll certainly need to navigate through that. And as we learn more over the course of the year, we'll certainly begin thinking about the longer term, and we'll keep you informed for sure.

Operator

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

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

So to Kevin's point and kind of your answer, it's clear, whatever you do from a membership perspective is going to be kind of dependent on what your peers do. I'm more interested in trying to understand -- I mean, by my estimation, give or take, you're probably slightly better than breakeven, call it, 0% to 1% margins in Medicare Advantage is implied in your guidance for 2024, correct me if I'm wrong.

But from there, it looks like your -- that $6 to $10 would be an additional 1%, maybe 1.5%, which then comes down to cutting benefits about $10 to $15. Again, correct me if my math is wrong here. I guess the question is, how do we arrive at that number? I look back over the last 6 or 7 years when things were good and senior store benefits increased by $20 a year, it looks like. And then when we see what feels like a 100-year storm, why is $13 to $15 the most we can put through? Why not try to get back to a target margin or closer to a target margin and assume you're -- if it's not company-specific, assume that the industry is going to follow? And if they don't, so be it.

Susan Marie Diamond - *Humana Inc. - CFO*

Justin, yes. No, those are all fair questions. And I would say directionally [assuming the] numbers, mathematically, you're right. So '24, what you're estimating for the margin is certainly directionally correct. As for the $6 to $10, one thing is important to keep in mind, that is what we're committing to in terms of earnings and EPS improvement next year. That would be on top of whatever rating action might need to be taken for the rate book itself. And right now, we are assuming that the '25 rate notice will look similar to 2024 in that it will be negative given we have another 1/3 of the V28 model implementation. So our assumption in all of this is that we will have some further pricing action to take to address just the 2025 rates and the fact that they will be insufficient to cover normal course trend. So that would be additive.

To the degree the rate notice is different and positive, then that could change our ability to extract more. But as we said, we need the benefit of the rate notice to fully assess that and are making what we think are reasonable assumptions at this stage. The other thing to keep in mind is with 1/3 of our book risk provider supported, while we will certainly take benefit actions across that book as well, it leaves some minimal impact to our earnings. And so the $6 to $10, you can think of as really having to be realized over roughly 2/3 of the book. So it does translate into a higher benefit reduction than your math would suggest.

And then I do think it's important to just remind everyone about our commentary this morning that to the degree '24 does, in fact, get better, we would expect that to be additive to that $6 to $10 going into next year because we do intend to price assuming this trend persists. And so if we see positive development over the course of the year, that would be additive and you would see further appreciation. And just given, again, as we said, the recency of these trends, we just are going to need some more time to fully assess that and the likelihood that they will persist for that period of time. But our intention is to be very diligent about restoring margins. And this is our best estimate at this time based on what we know with what we think are reasonable assumptions.

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

And just on that, Justin, what we are trying to do is be thoughtful around the profitability of the company, and we are committed to getting to restoring our margin, I want to say that. How -- if we do, we do that in 1 year or do we do that in multiple years is something that we're really addressing. As we've looked at the price elasticity of our members, we're really also trying to figure out where does it just fall off the cliff, as opposed to losing some members or not growing as much. So we are committed to pushing -- ensuring that we are going to move the margin. And at the same time, we just don't want to fall off the cliff and lose hundreds of thousands of members as a result of that. So it is just a question of timing as opposed to the question of trajectory.

Operator

Our next question comes from the line of Stephen Baxter with Wells Fargo.

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

So just another quick one on the magnitude of improvement in 2025. And I think when we looked at what your earnings trajectory was, maybe stepping back a couple of months ago, we would have already thought that you were going to improve earnings around $6 in 2025. So it's a little hard to feel like the incremental actions you're taking related to pricing honestly are really all that material. So I would love to just get a little bit more color on that.

And then just also your approach to operating expenses in 2024 and 2025, like it does look like you had SG&A up $700 million in 2024. I guess I thought there might have maybe more actions you could take to try to protect earnings in the short term as you work to reprice. I would love to just understand that a little better.

Susan Marie Diamond - *Humana Inc. - CFO*

Sure. So I'll take the operating question. I might need you to clarify your first question on pricing. But on the operating front, yes, as you saw and as we've been describing all year, as we saw the initially higher outpatient trend starting in the second quarter, we were able to successfully mitigate that pressure that we stepped up to through the third quarter through multiple levers, including administrative cost -- further administrative cost reductions. And you saw that in the operating cost ratio we reported for 2023, which was certainly favorable relative to the commitment we've made for 20 basis points of annual improvement.

We certainly continue to work very hard to identify additional opportunities, and our '24 guide reflects about 30-basis point improvement versus the 20 commitment, so demonstrating again, continuing to use that as a way to mitigate some of these trends. We do think there is additional opportunity, particularly leveraging technology, AI and some other tools, but we recognize they probably have longer timelines to get the full value realization. And so we will continue to build the pipeline.

And you should expect us, I think, to see better than the 20-basis point commitment over the next number of years, and we'll certainly work hard over the course of the year to see what potential we have through '24 and '25. On the pricing question, would you mind restating that, just to make sure I understand what you're comparing to?

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

Yes. Like I would have thought you would have, 2 or 3 months ago, been going from $31 of earnings to $37 of earnings, so already kind of delivering $6 of incremental earnings. So comparing that trajectory to the trajectory now, you're talking about kind of an incremental 0 to $4? Like that perspective is kind of what I'm trying to get at is, why couldn't you do more, more quickly to kind of accelerate the trajectory?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. So I think obviously, what we're dealing with is this higher trend, which is significant. And so when you think about over the course of '23, since the time of pricing, it's about $3 billion of additional trend that's emerged that we're having to absorb in '24. And again, our assumption right now is that will continue and will have to be absorbed in our '25 pricing. And so that is where we will certainly take as much pricing action as we can. We will have to see the rate environment, but there is a limit to what you can do in 1 year. And with that level of trend, which was never contemplated in the $31, there's only so much margin expansion you can get once you actually cover the trend.

Now over the long term, as Bruce alluded to, there are inherent mechanisms where it will work its way into the rate. It takes a little bit longer for the benchmarks to reflect the higher rates. So that is certainly something we'll see in the future. And to the degree any of this is attributable to higher acuity or condition development, et cetera, we should see that in risk adjustment over time as well. Those are all things that will take more time to assess, and we'll certainly consider. But for right now, with our assumptions for 2025 and the timeline, we'll have to cover the trend and then again, do as much as we can on the margin expansion as we committed to today.

Operator

Our next question comes from the line of Ann Hynes with Mizuho.

Ann Kathleen Hynes - *Mizuho Securities USA LLC, Research Division - MD of Americas Research*

Just thinking about the competitive environment. Obviously, it appears very challenging, and Humana seems to focus on profitability versus growth. But in a scenario that -- I think you mentioned in your prepared remarks, Bruce, that you hope that your peers would also price for 2025 given the challenging utilization environment. But if they don't and the environment stays like this, how do you view growth versus margin over the long term? And would you -- may not prioritize profit and be willing to grow below market? Or do you think you can eventually grow within the market again? If the competitive environment doesn't change.

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

Yes. Well, I think it's a big assumption that the competitive environment doesn't change, and I'll answer your question specifically, but I do want to just reemphasize that. What we have seen over the years, and we saw it in 2022, we saw it this year. There is one or -- usually one, maybe two that gets really aggressive and then they fall away the following year. And we've seen that over a long period of time.

And as you look at our growth over an extended period of time, you will see these volatilities year-to-year but that's really not a result of our pricing. It's more a result of the industry pricing. We usually have been fairly considerate in our pricing in the industry and have not been as aggressive as competitors, and there will be one or another one that comes there. We don't think that is sustainable. We just don't. We see the business as being much tougher as a result of regulatory environment, we see that things like what we saw this year relative to utilization, getting back to above COVID levels, we just see it not being as easy to price to membership growth.

I will say that from our vantage point is that similar to what we did in Part D, is that we'll continue to focus on what is the sustainable, profitable and the appropriate profitability within the industry, and we will price towards that and use our brand and our relationships with our value-based providers, our quality scores and other mechanisms to compete, but we do not feel that pricing is how you compete. You price to be economically solid and you price to be -- to provide value to your customer. But at the end of the day, we don't look at that as a competitive advantage. We look at our capabilities as a competitive advantage, and we'll continue to focus on the capability and the differentiation in our capabilities.

Operator

Next question comes from the line of A.J. Rice with UBS.

Albert J. William Rice - *UBS Investment Bank, Research Division - Analyst*

Just trying to get two things here. Your comment about inpatient utilization, I think up to this point in the commentary, you attributed a lot of the higher inpatient utilization you were seeing to that cohort -- the growth cohort of '23. It sounds like maybe that's broadened on. What are you seeing late in the fourth quarter, what gives you the -- what are you seeing seasonally that makes you think that continues? And by the way, did you keep a lot of those '23 cohorts? Or did they -- is that where we're seeing some of the growth, at least in one of the competitors that those people transitioned away from you.

And if I could just ask, in a normal environment where an MA provider -- a carrier has priced below trends, the natural result has tended to be that you get very strong enrollment. We're not seeing it this time. And I wonder, conceptually, how you put that in context that the fact that you're saying you're underpriced for the '24 trend you're dealing with, where that usually results in big enrollment growth, your enrollment expectations for '24 are quite modest. How do we put that in perspective?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure, I can answer that. So on the first, related to inpatient, you are correct. When we cited the inpatient pressure that we were seeing earlier in the year, we attributed that to the fact that we had a lot of new enrollment growth, and have limited information from which to predict the level of medical cost utilization. So risk scores is one example. And we were seeing that relative to our expectations, the medical costs were slightly higher than we would have expected based on what (inaudible) was indicating. So you were correct about that.

I would say what we saw in the fourth quarter is completely unrelated and different than that and very much more widespread. And particularly for the months of November and December. And what we've seen so far is an increase in short-stay inpatient authorizations, in particular. They are being upheld through our utilization management processes at a higher rate than you would typically expect as well. And given the positive seasonality you would typically see in the months of November, December, it was that much more surprising. The absolute level of authorization was up relative to what you would have expected for all those dynamics.

Coincidentally, and while the data is still very early, as you know, on non-inpatient, we're relying on the paid claims to get some visibility. We are seeing indications that starting in November, we are also seeing a decline in observation stays. So that's something we will continue to analyze and understand better. But quite frankly, we are going to need more time, more claim development before we understand the underlying sort of admission diagnosis codes and other things to fully assess the nature of the uptick in inpatient and corresponding decline in observations and understand if they're in any way related and then how we think about that again on a go-forward basis.

In terms of retention mix, I would say a little bit too early for us to fully assess that and look at -- we'll certainly look at the AEP enrollment data. I would say from what the teams looked at so far, nothing of concern in terms of the retention mix versus those members who disenrolled. But generally, I would say, given the benefit reductions we did make in '24, I would certainly expect individuals who have an intent to highly utilize those benefits were probably ones that were looking at what other options might be available. And to the degree another plan maintained a richer level of benefit, certainly would expect that, that was some place we would see higher disenrollment.

To your question about '24, so I would say it a little bit differently. While certainly, this trend was not fully contemplated in our pricing, I think the entire industry would agree with that statement. All of us saw unexpected trend after we filed our bids. We, in spite of that, though, did make more benefit adjustments than the industry. And so if you remember, we talked earlier in the year that when you look at the changes made, we did make a higher level of benefit adjustments than others. And in some cases, we were very surprised to see actual net incremental investment in '24 despite the Stars and V28 and other headwinds that they were dealing with.

So we don't feel like this is an issue in terms of underpricing. It's just the occurrence of higher-than-expected trend late in the year, unfortunately, after benefits were filed. And again, a lot to learn in terms of the persistency of that, not only through '24, but '25 that we will continue to evaluate as we do all of our 2025 pricing. But based on everything we know now, our intent would be to assume those trends persist and make sure it's covered in our 2025 pricing.

Operator

Our next question comes from the line of Ben Hendrix with RBC Capital Markets.

Benjamin Hendrix - *RBC Capital Markets, Research Division - Assistant VP*

I just want to get back to one more question on the $6 to $10 for 2025. I appreciate your comments on the overly competitive environment and difficulty in forecasting how actors scale that down in the future. But if you could comment on -- is there a level or a range of kind of headwind attrition that you were assuming in that $6 to $10? And if so, what are you expecting -- kind of margin versus attrition, [is it] kind of offset by attrition to kind of get you to that range?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, Ben. So we won't comment specifically, obviously, on expected membership growth at this stage, but just directionally can tell you that in the range of scenarios the team has reviewed and one of the reasons why it's a larger range as well, as I said earlier, is there's got to be an assumption around membership impact based on our changes as well as those of others across the industry. And so you can think of -- that range accommodates a less optimistic and more optimistic range with the less optimistic, assuming we do lose not a small number of members. So hundreds of thousands of members would be contemplating that low end of the range.

Some of that is going to depend on, as I said earlier, as we look at certain counties and plans, whether or not we think there is a path to the profitability levels we would expect. And there may be some cases where we -- at this time, we feel that's not true, where we might see disproportionate impact. You might remember years ago, we used to actually disclose sort of planned exits and how much impact there was to our membership growth. It's going to be akin to that, where if we do ultimately determine we need to exit counties or plans, we will probably disclose that discretely in terms of the impact. And I said you can consider that sort of no-regret move as a way to restore margin.

But our hope would be that we can find solutions to that and may need to moderate benefits and still provide a compelling value proposition, but recognize some areas will have disproportionate cuts, which will have disproportionate impact to membership. And certainly, as we go through the bid process and share updates with you later this year, can give you an updated perspective on where in that range we might be depending on what we continue to learn.

Operator

Our next question will come from the line of Nathan Rich with Goldman Sachs.

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

Can you hear me okay?

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

Yes, we can.

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

Great. I think following up on A.J.'s question. Susan, you kind of talked about still evaluating some of the drivers of utilization as it relates to '24. I guess maybe could you talk about what you're looking at specifically, I guess do you expect those dynamics you mentioned around the nature of hospital stays to continue? And are there any early data points on January that would suggest the higher trend that you saw kind of emerge late in 4Q isn't seasonal?

And then just as a clarification, you talked about restoring margins longer term. I guess, has your view of long-term margins for the individual MA business changed just given the backdrop that the industry faces?

Susan Marie Diamond - *Humana Inc. - CFO*

Nathan, sure. So in terms of the utilization drivers, as I said earlier, they are definitely shorter-stay events. We have looked very closely at the respiratory data. And as we said in our commentary, based on all the information we have, it is not respiratory-driven. As you guys might remember, we called out COVID in our third quarter call that we saw. And if you remember at that time, we hadn't anticipated in the third quarter in our original thinking but had them in the fourth quarter. And if you recall, what we said is despite the fact that it peaked in the third quarter and may come down, we left it in our fourth quarter forecast.

And so as we look at the fourth quarter results, while you certainly see an uptick, third quarter to fourth quarter in respiratory, that was something we had anticipated and was actually slightly favorable to what we had expected. We had planned for sort of a 5-year average on respiratory and it came in slightly lower. So for us, it was not a cause of the variance and the additional utilization is nonrespiratory related.

For that reason, because we don't have any clear indicators that it is something that you can reasonably assume as seasonal or transitory, we're making the assumption that it will persist throughout 2024. Looking at January data, which is very early. So we only have really some look into the first 2 weeks, we would say it is continuing to stay at the elevated levels that we saw in the fourth quarter. So -- and again, I wouldn't have expected anything this quickly to change that pattern materially, but it does reinforce that at least for the near term that we can likely expect to see it.

Again, we will continue to evaluate the more mature claims data to try to get more information about the drivers. One thing we're certainly looking at is if you remember, there are regulatory changes being implemented, January 1, related to utilization management, [referred visit], 2-midnight rule. We know there was a lot of activity both on health plans and providers that are preparing for that. And so that is one thing we'll be looking at to see if potentially that has any underlying cause related to some of what we're seeing based on what we had expected for '24.

In terms of the long-term margin outlook, I would say we had -- if you remember at Investor Day, we had really moved away from setting a specific target for individual MA, recognizing that we will work very hard to maximize the margin contribution across the enterprise. Which becomes increasingly important as we continue to expand and scale the CenterWell capabilities. And so we remain very focused on that. we will certainly expect, as we said, to restore margin to a reasonable level within the health plan over a relatively short period of time. But you will hear us continue to emphasize the opportunity to expand enterprise margin over just discretely focusing on the health [plan] growth consistently going forward.

Operator

Our next question will come from the line of David Windley with Jefferies.

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

Continuing on the last one regarding utilization. I guess, in your scenario analysis, Susan, to what extent are you taking into account the possibility that utilization could go higher again from here? Or what kind of boundaries or historical norms could you frame for us to judge the likelihood or unlikelihood of that?

I'm also wondering, in your pricing model for 2024, to what extent did Humana reduce benefits to offset the risk model change in pricing versus how much of that did you -- were you willing to absorb in MLR for '24? And then finally, was there a difference in this utilization between regular community MA and duals?

Susan Marie Diamond - *Humana Inc. - CFO*

David, yes, I'll take that. So on the utilization, as we thought about 2024, as we said, we have assumed that these higher costs will continue throughout 2024. So think of it as your new baseline. We have then applied, what we said, our normal course trend on top of that in our estimates. And so this late in the year, we obviously have visibility to CMS rate changes on unit cost and a variety of other specific inputs that are specifically accounted for, things like leap year. So all of those things are accounted for. And then embedded in what we consider that normalized trend is an assumption that we will see incremental utilization trends in 2024 on top of this higher baseline.

I would say internally, that has been the biggest source of debate. And to what degree you will see continued utilization trend on an outlier level of utilization trend in 2023. But again, we wanted to be as prudent as possible in terms of the assumptions we made in the guidance we provided today. And so that has been included in our estimates and something we will continue to watch. But I would say it's probably the biggest source of variability. I can't sit here today and say there's no way it can be higher, right? I'll just jinx this if we do. So we'll just continue to watch it. But I will say, given the level of utilization we've planned for, it would be, I think, surprising to see something of that magnitude on top of what we saw in 2023, but we'll have to continue to watch it.

As with respect to our '24 pricing, we did obviously have the knowledge about the V28 changes. There's certainly some estimation you have to make as part of that because you're having to predict sort of the progression of diagnosis codes into the future. But that was all baked into our 2024 pricing assumptions. And one of the reasons you saw us make actual benefit reductions in '24 because with that adjustment, the reimbursement was going to be insufficient to cover the annual trend. And so that is one of the reasons you saw that.

In terms of duals versus non-duals, with the pressure we're seeing this year. I would say the more recent pressure -- earlier in the year, I would say less on the dual (inaudible) then non, but I would say some of this inpatient pressure, we are seeing more broadly and maybe even a little bit more on the D-SNPs versus non-D-SNPs. But again, there's a lot more run out. We'll need to see, particularly on the non-inpatient side, to ultimately do some of those both plan-level and member-level cohorts to understand exactly how the plans and cohorts are being impacted.

Operator

Our next question will come from the line of Scott Fidel with Stephens.

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

Actually, first part just might be helpful to tack on to Dave's question. Just -- can you actually share with us what you're estimating, Medicare or MA sort of underlying medical cost trend was in '23 and then what you're predicting it to be for '24?

And then sort of the other sort of question I want to ask you is just back on the competition discussion. Hopefully, you can be a little transparent here and sort of be -- in how you see how extensive this competition is right now in the market. I think there's a lot of focus on one large competitor who's sort of taking all the market share in the industry in '24. Wondering sort of when you think about that intense competition, how much of it is that one large competitor? Or how much more broad-based is this beyond just that one competitor?

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

Scott, I'll take the competitor side and then let Susan take your other question. Obviously, this year, it's one large competitor. As you look at our sales and where we are compared to the -- to all the competitors, we've finished second behind that, the larger competitor, but a very distant second.

And as I mentioned before, Scott, and you've seen it over the years, we do see this behavior that there's one that sort of stands out and takes share for the inappropriate reasons around price. There are smaller players in the marketplace that maybe impact us in one market or another, but I wouldn't get overly upset about those. We see those come and go. We just see one this year. And we suspect that for all the reasons that we've discussed this morning, that player will readjust in 2025.

Susan Marie Diamond - *Humana Inc. - CFO*

And then, Scott, with respect to your trend question, so we have not historically shared absolute trend percentages. The one thing I will comment on, just because we have provided a commentary throughout the year, we said earlier in the year as we were watching the non-inpatient and the outpatient in particular. We mentioned that we were seeing high single-digit trends throughout the year. I will say, once we got to the final full year numbers, we are slightly above in the double-digit range, unfortunately. So that continued, as we said, to be high and sequentially uptick. And so that I can be a little bit more specific given the commentary.

I would say, in the aggregate, though, what I would say is I would think about it by looking at our MLR, you can assume that the majority of our MLR variance is obviously attributed to the higher trend. And so you saw, obviously, in the fourth quarter, 190-basis point miss in the quarter and the translation of that to the full year. And then as you saw in our guide this morning, you can see the 200-basis point year-over-year increase in MLR, which you can use to sort of get a rough estimate of how much the trend increased as that's the main driver of that change.

Operator

Our next question comes from the line of George Hill with Deutsche Bank.

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

Yes. Can you guys hear me okay?

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

We can.

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

Okay. I guess, Bruce, I kind of want to step back and ask you a couple of questions around margin. And I guess, I don't know if you guys are able to comment to the margin profile that you guys expect to price to for 2025.

And then I would also ask kind of from here going forward, what do you think is the rate margin profile for the MA plan business? And how is this impacted by whether or not your competitors you think want to subsidize the other parts of their business where they monetize beneficiaries either in care delivery or in pharmacy versus monetizing the members at the plan level, just to kind of be very interested in kind of how you're thinking about plan margin versus like, what I would call it, the total value of the beneficiary?

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

Just on the margin side, I don't want to get into a specific number, maybe a little more philosophy, but we do want to restore margins where they are profitable and contributing to our business in the proper fashion. And I would say, historically, that you can pick the years out, you've seen that. But we do continue to reemphasize the enterprise earnings as an organization, and we look at the value that we provide across the organization, not only to our shareholders but also to the individuals we serve.

And we do find that the growth and the scalability and the integration of CenterWell offers us that opportunity to continue to expand not only our services that we find are much more effective in clinical outcomes and satisfaction, but also the ability to continue to drive better and better value for the enterprise overall. How those get repriced into the actual product itself, we'll look at, but we really make two separate decisions there. One decision around, is this the right both competitive and profit profile that we look into the plan. And then in addition, we also look at is this the right value that we provide on the CenterWell side and look at that.

For our competitors and their pricing and getting subsidized, I'm not -- probably -- right now, I'm not seeing a significant change there. I'm seeing much more -- because there's not -- there's some in-sourcing that's going on. But I would say that material orientation is more around market share gain and membership growth and really using the plan for that. So we don't see a disadvantage in the markets that we're competing in that are pricing as a result of something that's happening as a result of subsidization. We really view the ability to continue to drive the membership growth in the total value of what we offer, and that's around our brand, our quality and in addition, the relationships that we have with value-based providers and feel that, that will carry the day for the foreseeable future.

Susan Marie Diamond - *Humana Inc. - CFO*

And George, to your specific question...

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

Maybe just a real quick -- go ahead -- Susan, just maybe then a really quick follow-up would be just how do you guys think about enterprise margin? And then how should investors think about enterprise margin versus plan-level margin?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. And so just real quick on your specific question on the '24. Justin made the comment earlier about the implied margin in 2024 which we said is directionally correct. So even assuming that the majority of the EPS improvement we've committed to next year is going to be driven by individual MA. And so you can sort of make -- do that math and get a sense for the -- where we'll end up after '24.

The other thing I would say to you is with the targets that -- growth targets across the industry, I would argue that in order to achieve those in the size and scale of these books, you're going to have to expect both progression on the health plan and the services side of the business versus completely bringing down the health plan for the sake of all of the other ancillary benefits. So I think that you'll see progression on both.

The other thing I would point out is as we think about 2025 and the benefit adjustments we're going to have to make, we are being very intentional around which markets do have further integration opportunity and where we have CenterWell assets, particularly primary care. And I think you will see us prioritize those markets to ensure that we can drive disproportionate growth in those markets to a greater degree going forward and support that enterprise integration and margin expansion that we've been talking about.

We don't intend to set a specific target in terms of enterprise margin, but rather commit to the long-term sort of EPS growth rate. And certainly, we'll provide more clarity on that going forward, recognizing we're approaching 2025, after which we'll have to give you some updated commentary on what you can expect going forward, which we would expect to do later this year.

Operator

Our next question comes from the line of Joshua Raskin with Nephron Research.

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

I just want to get back to the 2025 range of $22 to $26 per share. And if you view that as a reasonable baseline for what Humana can earn on the current book of business with your current assets or are you suggesting that there are additional years of growth in EPS above your long-term target behind that?

And then, I guess, more importantly, if that is the baseline that you guys are working off, has the management team and the Board thought more about the benefits of even larger scale of being part of a large and more diversified entity? And maybe you could talk about what you think the benefits of that would be.

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

Josh, I would say that we don't look at the baseline for -- we don't look at 2025 to be the baseline. We look at that there needs to be continued -- more improvement in that as a result of what we believe is a profitable -- the appropriate profitability for the organization. And as Susan mentioned, we do want to get back to the earnings growth that the organization deserves as a result of the industry we're in. And in addition, as a result of the total addressable market and the expansion of that.

In regards to the size and scale, we constantly are asking questions like that strategically. And today, we have -- and we feel continuously that our ability to be best-in-class in the industry that we compete in is really where we drive towards. And I think you've seen that in multiple different levels, as I mentioned, quality to our relationships with our providers to just the ability to have an integrated model that serves one population. And we feel that that's a large advantage.

We also feel especially through our productivity efforts that we've had over the last number of years that our cost structure continues to prove itself out relative to the ability to improve our cost structure through a sustainable model. But I do want to reemphasize, the Board and the management team constantly has looked at what is in the best interest of the shareholders. And we're not -- we will continuously do that. And if at some point in time, that question becomes a question that we need to take action on, we'll definitely take it or if it is -- ever comes and is presented to us. But we do believe today, being a specialty player in the fastest-growing part of the industry is the best value for the shareholders.

Operator

Our next question comes from the line of Lance Wilkes with Bernstein.

Lance Arthur Wilkes - *Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst*

Yes. Can you talk a little bit about two aspects of the forward-looking pricing adjustment. One would be for the pricing assumptions for '24 and the -- or the 200 basis points of increase in MLR, is that also a 50-50 inpatient-driven variance to your prior expectations? And half of it not related to that? Or is there something different there?

And then from the inpatient experience you saw in November, December, can you talk a little bit about -- for the short stays, are there particular types of members that you're seeing that disproportionately on, and a little bit of why you weren't able to identify this a bit earlier? Is this something that would naturally have some sort of upfront insights from prior ops or things like that?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, sure. So in terms of the MLR increase in '24, I would say, given the -- the recency and the magnitude of the inpatient trends, which were really the large -- more unexpected in the fourth quarter, as you think about the revision to our forward outlook, I would say it's probably disproportionately inpatient-driven. And Lisa, I can certainly follow up and if -- we'll go verify that and then get back to you if there's anything different. But I would say it's probably more disproportionately inpatient-driven, given it was really the last 2 months of the year and then have to carry that forward through the entirety versus the non-inpatient which we were seeing upticks over the course of the year. And anyway, so that's my thinking there.

On the November and December, I would say on the inpatient side, again, seeing it more broadly, as we said in the commentary, we are seeing less of that, though, in our Florida HMO market in particular. And we are seeing some differences in the results of our utilization management against this higher trend in different geographies. So that's something we are certainly looking at to see what we can learn from and if there's any additional opportunity more broadly based on the outcomes we're seeing in the Florida market.

And to your question of why we maybe -- could we have predicted it. I would say on the inpatient side, as Bruce said earlier, these are really unprecedented levels of trend increase. And I would say the pace at which they changed as well. We do leverage authorization data on the inpatient side. We are actually using that to actually book reserves each month. We get authorization data for over -- like 99% of the inpatient events that occur. So it's very accurate in predicting, and we do receive it in more real time.

The non-inpatient is where we are relying on claims and generally relying -- at least a 60-day lag to view those claims as credible. So with the December-paid claims, much greater visibility to October and prior dates of service. And based on that, I have to make some estimation for November and December, which, again, we've assumed those higher trends that we've seen will continue for the duration of the fourth quarter.

But we do leverage all the information you can get in real time. It is something we continue to look at. And we've been asked about over the course of the year whether there's more we -- say, surgical as an example. And we do continue to take ground to improve the level of authorization data we get for some of those things as well. It's just not sufficiently high to be credible for purposes of booking claims and estimating that at this time.

But I think, certainly, in light of what we've experienced this year, we're doing a lot of work to assess where there might be opportunities to improve analytic and forecasting models, whether we can leverage interoperability to get some greater visibility into provider utilization and a number of other things that we will continue to prioritize to make sure that we could continue to improve all of our forecasting work, recognizing it's inherently difficult given the nature of the program.

Operator

Our next question comes from the line of Whit Mayo with Leerink Partners.

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

Can you hear me?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes.

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

Yes, sorry it went blank for a second. Bruce, I'm just curious, looking at your partnerships with the various capitated medical groups that I think you said cover 1/3 of your book now. Obviously, we're seeing a lot of challenges in that market. They're feeling this utilization pain. What are the conversations like that you're having there? Are they -- any desire that they have in trying to carve out some of the risks they're taking on certain benefits, OTC flex cards? Is there any risk that you see that maybe you bring more of that back on your P&L, at some point, they could be a headwind?

And my other question is, I'm just wondering now that you've shut down the commercial business, is it possible that, that's having any impact on your network or rates that could impact your unit costs going forward?

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

Yes. The latter question I'll answer, the majority of our rates are predicated on Medicare rates. And therefore, it's not much of a negotiation. There might be a market here or there that we negotiate rates on, but -- in some way, but I would say that Medicare rate really determines our payment mechanism there and the commercial book of business, and we were very thoughtful in analyzing that and understanding that. And it has -- had no impact relative to our relationships with our providers.

And our providers that are taking risk, I do -- we do see a number of them having challenges as a result of this. And to be honest with you, we're going to probably see more. We have seen these challenges over the years. We don't feel that's a headwind for us because we'll adjust the benefits and that will flow to them in a positive fashion.

And we are seeing a number of our better-performing providers really taking V28 and we're assisting them in what they can do to manage through V28 and taking our learnings through the CenterWell and offering that. But I wouldn't consider that to be a headwind for us going forward. But I do feel as we look forward that there will be some challenging times for the less sophisticated ones, and that could be an opportunity for us as we think about CenterWell.

Susan Marie Diamond - *Humana Inc. - CFO*

And what I would say as well -- and I have been saying this early in the year and more so now, I do think that as risk providers fully absorb the impact of V28 as well as this higher trend, I imagine that there will be increased discussions and pressure for the industry to appropriately reflect those trends in the benefits. As we said, we cut benefits more than anyone. So I think -- there may be some other payers having discussions with providers around some frustration over the level of benefit investment. Our primary care organization is having some of those very same conversations. And I do think there'll be a push from the provider community as well for discipline and balance given that we have further implementation yet to go with respect to V28. So I think that will be a positive. And hopefully bring the pricing discipline that we're all looking for.

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

And I think just building on Susan's comment there. What we do see is in some of the higher-risk areas like Florida, for example, we see the value that is offered to be much greater to the member than it is in other areas. And therefore, we feel that the adjustment for the -- for the particular benefits in those marketplaces has much more room than, say, in the middle part of the country. And so we do see benefit adjustments needed in that marketplace, and there is opportunity as we look at the value proposition from a member's point of view.

Operator

Our next question comes from the line of Gary Taylor with Cowen.

Gary Paul Taylor - *TD Cowen, Research Division - MD & Senior Equity Research Analyst*

I wanted to go back to '25 just for a moment, make sure I'm understanding. It looks like the earnings pickup is implying insurance segment margins would improve 100 basis points, maybe a little bit more. And I know the Street simplistically assumes you can always just cut benefits to hit your target margin, but the CMS TBC change thresholds do handcuff you to some degree.

So is the right way to think about '25 is right now, you're assuming a negative rate update? I'm sure you're probably assuming some positive cost trend growth in '25. You'll need to use a portion of your TBC threshold just to solve for that math. And then the 100 basis points implied margin improvement, earnings improvement is really what's left to be recovered after that math? Is that a good way to think about -- with due respect for your capitated arrangements as well? Like is that the right way to think about kind of how much you're delivering to shareholders in terms of margin EPS for '25?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. Gary, so you're thinking about the math right. And as I said earlier, we are anticipating that the rate notice in '25 will look similar in terms of impact to '24 as an initial assumption. If you remember, we cut about, on average, something close to $13 on average PMPM in that environment. And so that, you can think of as your baseline in terms of just from the rate notice.

Then what we've committed to from the earnings [appreciation], if all of that really came from individual MA, even you can do the math in terms of what the average benefit cut is, which should be incremental to that rate notice. Once you account for (inaudible), you are really bumping up against that upper bound of what's possible. And that's why it's also important to remember that range also contemplates some level of membership impact as a result of those cuts, and that is a huge input as well that we'll continue to refine once we have a better understanding.

So I just want to make sure we're leaving everyone with the impression, we are taking significant pricing action in order to deliver these results. We will continue to evaluate the trends and to the degree they get better, that provides them more opportunity. We will work hard to optimize within the bids and themselves to make smart decisions such that we maximize the impact and maintain a really compelling value proposition still for consumers on a go-forward basis. But we think with the reasonable set of assumptions and the dynamics in play, the $6 to $10 is really bumping up against what you can do in the absence of something changing between now and when we [estimate] pricing that we can incorporate.

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

And Gary, I just want to reemphasize something here that we also are very active in looking at a trend offset. And we have a lot of activity going in the organization around that. And we are oriented to how can we get a number of these things through other -- both clinical actions and then also just the proper insurance that people are using the health care system most efficiently.

Susan Marie Diamond - *Humana Inc. - CFO*

And Gary, I think that's why, as Josh asked Bruce earlier, we do think it's probably a couple of years of recovery to get back to the margin profile just because of the inherent limitations and expectation that the rate environment won't fully cover trend, and that has to be addressed as well.

Operator

Our next question comes from the line of Sarah James with Cantor Fitzgerald.

Sarah Elizabeth James - *Cantor Fitzgerald & Co., Research Division - Research Analyst*

I was wondering if you could give us more color on your claims clarity. So you made some comments earlier about waiting for more November claims clarity. And that sounds a little bit slower than I typically think of the industry getting 60% of the 30-day claims and 80% of the 60-day claims. So how much clarity do you guys have on November and December? Was there any kind of slowdown this year?

And as you think about that going forward, there's some regulatory changes coming around having to do prior authorization in 72 hours or make decisions in 72 hours. Is there a potential that, that could have an impact on your claims clarity when that goes into effect in '26?

Susan Marie Diamond - *Humana Inc. - CFO*

Sure, I'll try to answer those. So in terms of claims, as we've already said, we had more visibility real-time to inpatient utilization from the authorization data that we receive in more real time. We're dependent on claims data to understand the unit cost of those inpatient events and get more details on some of the underlying (inaudible) and condition data and other things to understand the acuity and the level of treatment and intervention.

On the non-inpatient side, while we do receive authorization data for some of our service categories like outpatient surgical, it is not sufficiently high to be credible. I think -- and we've made improvement over the years, but I think it's in the order of magnitude approaching [60%] of those events, but we have demonstrated through an (inaudible) that is not sufficiently credible to base your claim estimate off of. So we will certainly look at it as an input. But for those categories, we are very much relying on completion factor models based on paid claim progression.

I will say, we certainly -- while we don't rely on the most recent 60-day paid claim data, we certainly do look at it. And in fact, for the month of December, we did see very high levels of paid claims for dates of service for December, which would be atypical. In light of what we saw, we did step up to an assumption that some of that will result in higher costs. That was primarily in the physician cost category. So we've accounted that for that in our year-end estimates, and that's what we'll just have to see as those claims be more fully mature, how that develops, but did our best to make sure that we were using all of the readily available information to base our year-end reserves.

On utilization management, as you said, there are changes anticipated for 2024. We knew that at the time of pricing. We did have an expectation as a result of those changes that we will see a larger number of inpatient authorizations approved where in the old model, they may have been downgraded, say to an ER or observation event or denied for medical necessity. So we do anticipate a meaningful impact to inpatient utilization trends as a result of that, and that was accounted for in our initial pricing and our initial thinking and targets for '24.

We will have pretty good visibility in near real time to how those utilization management outcomes from the initial assessment are holding up versus our expectations. The piece I will say will take a little bit longer to assess is do we see any subsequent change in provider appeals or ultimate uphold rates. Those will take a little bit more time. Again, we use our best judgment and data to make some assumptions about that. But that, I will say will take probably throughout the first half of the year to understand if there are any unanticipated changes to those appeal and ultimate uphold rates. And we'll certainly keep you guys informed if we see any variances.

Operator

I'm showing no further questions in queue.

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

Okay. Well, I'll close out the call here. And as I started the call, we are disappointed in the update provided today. And as I've said many times, we take our commitment serious, and we'll continue to work hard on behalf of our investors.

I do want to first just continue to reemphasize that although the near-term impacts of the higher utilization are disappointing, our confidence in the long-term attractiveness of this sector and our position within it has not changed one bit. I do want to say thank you for both your time today and our 65,000 employees for their dedication and support for our business and the individuals we serve. So thank you, and have a wonderful day.

Operator

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