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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good day and thank you for standing by. Welcome to the Humana third-quarter earnings call. (Operator Instructions) Please be advised that today's conference is being recorded.

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

Lisa Stoner - Humana Inc - VP - IR

Thank you and good morning. I hope everyone had a chance to review our press release and prepared remarks, which are available on our website. We will begin this morning with brief remarks from Jim Rehtin, Humana's President and Chief Executive Officer, followed by a Q&A session where Jim will be joined by Susan Diamond, Humana's Chief Financial Officer; and George Renaudin, President of Humana's Insurance Segment.

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 third-quarter 2024 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 at 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. And 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. A 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 Jim Rehtin.

Jim Rehtin - Humana Inc - President, CEO, & Director

Thanks, Lisa. And good morning, everyone. Thank you for joining us. In the last quarter, I outlined four basic drivers of our business that we need to be able to deliver against over and over again. Those are, first, providing a Medicare product and experience that delivers against consumer needs and is priced with discipline. Second, it is operating with clinical excellence. This really is the foundation of industry-leading margins. It is, third, managing a highly efficient back office; and its fourth, deploying growth capital in a way that complements our Medicare Advantage core business, but really focused around CenterWell and Medicaid.

I'd like to review the quarter's results with a little bit of a lens towards those four drivers. Before I do that, let me just start with a few headlines. First of all, as we noted, we exceeded expectations for the quarter. We're also confident that we will achieve at least \$16 of EPS for the full year, and we are comfortable with where 2024 EPS consensus sits today. Exactly where we're going to land is largely dependent on a number of investment decisions in AEP and in Stars that we continue to evaluate.

We also feel good that we priced our MA product for margin expansion of 2025. However, similar to our strategy for the rest of 2024, we will be balancing near-term earnings progression with investment in the business. And when we say investment in the business, certainly that is Stars, but it's also looking at investment opportunities and growth, admin cost efficiency, and medical cost management.

We understand that investors would like more clarity on the multi-year outlook of the business, and to address this, we are targeting an Investor Day in May of 2025. So let me turn to the four basic drivers for a moment. So right now, if I start with product and experience that we are delivering through our Medicare product, we're feeling pretty good about what we're delivering. And let me point out a couple of things.

Our individual MA membership growth continues to outpace our expectations for the year. We anticipate at this point full-year growth, year-over-year growth of around 5%. The year started slowly in AP last autumn, but we've made pretty significant gains over the course of 2024. When we look at it, we believe that this is a reflection of disciplined product pricing that has allowed us to continue to emphasize growth at a time when others in the market have pulled back.

And we also attribute some of the growth to incremental marketing investments that we've made in our internal sales channel. This is a channel that we believe is increasingly important for us, and those investments have been paying off. We continue to deliver best-in-class service. Recently, we were ranked the number-one health insurer for customer experience by Forrester. This is now four years in a row of being ranked number one by Forrester. And finally, while it's early in this year's AEP cycle from what we can tell, sales appear to be generally on track with expectations.

Turning to the second driver, clinical excellence, let me start with Stars. We've acknowledged now that we've got work to do to get back to the results that we expect of ourselves and that we expect for our members and our patients and our investors. We've been moving quickly to make investments and to align incentives in our provider and pharmacy networks to close more gaps in care. We've also redirected care management and call center capacity to increase member outreach, and that is also related to gaps in care.

Just last week, those efforts resulted in about 5,000 incremental primary care appointments. And I learned last night that we've got about another 3,000 to start this week, 3,000 primary care appointments scheduled. We're also making technology investments. This includes improvements to our plan finder capability. And really, the way I'd characterize it, we're on a sprint to take ground and to impact 2027.

And I simultaneously feel good about the team's focus and the effort and the impact that we're making, and frankly, frustrated that we have allowed ourselves a shorter runway than we would like to make up that ground. Clinical excellence also translates to lower cost when we deliver better care. And so in Q3, medical costs are largely in line with our expectations. There's obviously some give and take across categories.

The environment is still dynamic, and we will be careful with our expectations around medical cost trend. However, right now we are seeing some success in a number of our cost control efforts. The example I'll give is we've been extending value-based care contracts beyond primary care into areas like kidney disease and oncology care management, and we're seeing good results from that effort.

Shifting to the third driver, highly efficient back office, we do continue to make progress in this area. We're expecting a 30-basis-point decrease in our adjusted operating cost ratio for the year. And just to give one example of the type of work that is helping to drive this, we're implementing more and more uses -- use cases for AI. We recently launched a generative AI solution that allows our care management team to spend about half as much time on post-call documentation. They are still doing all the same human oversight for any clinical decision-making, but they're spending less time on documentation.

That brings us to our final driver, deploying growth capital to drive efficient growth. I would argue that we're quietly building the leading senior-oriented primary care organization in the nation. Our primary care clinics are hitting their clinical and their financial targets. They're on track to mitigate V28. We recently released a study in collaboration with a leading researcher and professor from Harvard that demonstrates both the clinical and economic value the clinics create.

It found that our members have a better experience when they are part of a senior-focused primary care clinic. We expect to add another roughly 40 clinics this year. Often, this is through acquisition of underperforming clinics that we've demonstrated we can pretty rapidly turn around. And our patient growth continues to outpace expectations.

I'm encouraged by our recent performance trajectory and growth, absent our Stars performance in BY26, and at the same time recognize that these continue to be dynamic times for the industry, and I believe it's critical that we continue to strengthen the organization by making investments to drive long-term shareholder value. This is obviously a balance with how we think about short-term earnings progression.

We look forward to providing formal 2025 guidance on our fourth-quarter call. And we will also look forward to providing a more fulsome update on our strategic initiatives and their expected impact at Investor Day, which again, we're targeting in May of 2025. Finally, I'll just say, look, our conviction remains high regarding the positive outlook for MA and for value-based care.

And with that, we will turn to Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Justin Lake, Wolfe Research.

Justin Lake - Wolfe Research LLC - Analyst

Thanks. Good morning. I wanted to ask about your comments on 2025 and specifically your comments on investment spending. Prior to this call, you talked to a margin improvement in MA next year, and combined with top-line growth, I think the expectation in the market was for \$2 to \$4

of improved earnings year over year. Given that you're talking about now, more flattish, that would seem to put that investment income spending or investment spending, I should say, at \$500 million, give or take.

Is that a reasonable ballpark, number one? Number two, can you give us some more color in terms of what you're spending that on, given you had just cut admin spending pretty dramatically over the last two to three years? Is there stuff that you overcut and you have to bring back? And then, how should we think about that rolling forward? Is there going to be a return there where it kind of nets to zero because you're going to get improved Stars, or what have you. And over what timeframe does that happen? Thanks.

Jim Rehtin - Humana Inc - President, CEO, & Director

So Justin, thank you for our first four questions. This is Jim, I'll start, and then I'll let Susan jump in. So let me just start with 2025. And I recognize that we're not going to be able to answer everything people would like. Obviously, we're going to give guidance here in a few months. But I'm going to try to be as clear as I can in what we are saying and what we aren't saying about 2025 right now.

The first thing I would just re-emphasize is we told everybody we felt good about our bid, meaning both our pricing and our plan exits, and what we're essentially saying is, hey, we're reaffirming that. Even after you incorporate the things that we've learned since the bid season, we still feel good about where we're at with our product. The result of that is that -- look, at a minimum, we see a 2024 performance as a floor as we head into 2025. In other words, we have room for EPS progression.

What we're also saying is we do need to see some things unfold over the next few months to establish how much room is in there. Whether you think about AP results, both the final member count and member mix, as well as thinking about continued monitoring of medical cost trends, the better visibility that we have into those things, the more confident and precise we can be in where we think we'll be next year.

We also are telling you, in fact, that just as importantly, we're going to be approaching 2025 with a similar posture to how we've approached the last quarter or two. Where we can make good investments to put ourselves on better footing in 2027, we're going to do that. And we're going to prioritize leaning into that long-term earnings potential over near-term EPS progression where we have good investments to make, but we're going to do that with a floor.

I would love to tell you that we've got precise numbers on all of those choices and decisions. We don't. Some of that is still in flux. And in some cases, we're actually making smaller investments. And as we see those generate returns, we're doubling down on it. And so we don't have a precise number today. What we're making sure is that we're creating room to make the right decisions for 2027 in the long term. But we're telling you we can do that while establishing the floor.

So again, I recognize everybody would like more clarity. I really do. And I want to reiterate that we're kind of trying to balance or focus on two things. Given the dynamic in the market, we want to be appropriately prudent and make sure that we're doing the right things to establish targets, hit those targets, build credibility over time. And we are trying to establish the best way to navigate through the next 24 months. I mean, that's really the two things that we're trying to balance here as we try to give -- set expectations the best we can.

Susan, what would you add to that?

Susan Diamond - Humana Inc - CFO

Yes -- no, I think that says it well. The only thing I might add is, Justin, that as we've begun to talk about some of the investments that we believe are needed, both for Stars but also to improve for operating performance, given some of the benchmarking work that we've done, we got some questions and concerns. Well, gosh, could the level of investments cause you to go backwards year over year?

So I think that was one of the reasons that we wanted to introduce the floor for '25, just to make sure that it was -- and so we're prepared to give formal guidance that we made it clear that we felt like with the pricing action we did take in the '25 bids, that did give us the room and flexibility to make these needed investments while not creating a situation where we might go backwards.

Operator

Ann Hynes, Mizuho.

Ann Hynes - The Mizuho Financial Group, Inc. - Analyst

Hi, good morning. So your MLR results imply trends were relatively stable sequentially. Is that a good characterization? And if so, what does this mean for your 2025 bids? Are they tracking in line or better than your expectations? Thanks.

Susan Diamond - Humana Inc - CFO

Yes, Ann. So as we saw the results develop for the third quarter, as we said in our posted commentary, current-year claims did develop as expected in total for the MA business. There were some geography differences in terms of seeing some improvement on the inpatient side, some slight deterioration on the non-inpatient, but in total, in line with expected in terms of claims development through the third quarter.

As Jim mentioned, as we continue to evaluate emerging trends versus what we expected at the time of bids, we continue to feel confident in how we've approached the trend assumptions within our pricing. Again, some geography differences, both across claims and risk adjustment, as we've talked to you guys in prior quarters, but in the aggregate, continue to feel good about the MLR that we would have been targeting inherently within our bid.

And as we also mentioned, at least based on the early information we have access to, continue to feel like our assumptions around membership for next year, meaning the loss of a few hundred thousand members, continues to feel like a reasonable assumption.

Operator

Andrew Mok, Barclays.

Andrew Mok - Barclays Bank PLC - Analyst

Hi, I wanted to follow up on the 2027 margin target and how you're thinking about the Stars recovery in the context of that 3% target. One, is that a realistic goal with the elevated investment spend and where your Stars scores fit today? And is there a minimum bonus level that you have in mind to deliver on that target? Thanks.

Jim Rehtin - Humana Inc - President, CEO, & Director

So I want to make sure I captured the question. So let me just play this back real quick. I think what you said is focus on 2027 is the 3% margin target, a realistic target at this point, and then what does that assume around Stars progression basically, right?

Andrew Mok - Barclays Bank PLC - Analyst

Right. Is there a minimum level you need to recover in order to deliver on that target?

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes. So 3%, look, I'm going to talk a little bit out of both sides of my mouth on this. 3% is realistic and there is risk to that number. And so we just want to be super clear. We're going after it. We're doing everything we possibly can to get to that point. And in light of Stars, yes, there is risk to whether we will get all the way there in 2027 or not.

We have to make meaningful Stars progression is the way that I would describe it. We're not putting a specific number on it. There are too many puts and takes across different variables in the business to try to put a specific number on it. But yes, you're going to have to make some meaningful progression in Stars to get there.

Susan, what would you add?

Susan Diamond - Humana Inc - CFO

Yes, I agree with that. And then the other thing, Andrew, that obviously, the right environment, the competitive environment, those are all things that, as we say, every year will also be important. As you know, '27 is the year where we'll have V28 behind us. Hopefully, IRA will then at that point be a very good guy versus a headwind.

And so there are -- there's an environment hopefully where you do have the room to take some additional margin, which we've talked about. But those will be variables that we'll have to consider. And then I would just say, some of these investments that we've been discussing now should pay off in terms of returns over that timeframe that also support that continued margin recovery.

Operator

Ben Hendrix, RBC Capital Markets.

Ben Hendrix - RBC Capital Markets - Analyst

Thank you very much. You flagged higher specialty drug costs within the non-inpatient utilization for the quarter. One of your peers noted a pull forward of some specialty drug utilization ahead of Part D changes next year. Is that something you would expect would be priced for as we head into 2025, or is there a component there that we should assume is a headwind for MCR modeling? Thanks.

Susan Diamond - Humana Inc - CFO

Hi, Ben. Yes, as you said, we did see some higher oncology costs in particular. I did call that out as something we were seeing in a conference I was at in early September. So we have been seeing it for a bit. We would say that our view is that it is not really largely attributable to IRA changes. They were relatively minimal in '24 in terms of member out-of-pocket exposure.

And so what we have seen so far is that we believe it's mostly attributable to either new treatments that have come to market or label expansions around existing treatments. And what we're seeing is, in some cases, these new treatments are being added to existing therapies, resulting in net higher unit costs than we've seen historically, and higher than we had anticipated as we evaluated the pipeline.

We do anticipate that we will see some further uptick in trends next year, just given the IRA changes and the introduction of the much lower maximum out-of-pocket. And so we have built in induced utilization assumptions into our '25 thinking, as well as just, again, continued sort of expectations around the emergence and uptake of some of these new therapies. So we have considered that.

Obviously, with IRA, there is more exposure on the plan side in '25, which is why we said you can expect that we'll start -- we'll take a more thoughtful approach in terms of our early guidance around some of these things that we can see how the trends emerge relative to your expectations in light of IRA.

Operator

Sarah James, Cantor Fitzgerald.

Sarah James - Cantor Fitzgerald & Co., Inc. - Analyst

Thank you. I was wondering, if Stars stay where they are, how much crosswalk is possible in 2026, given how you think about geographic overlap and plan ratings? And then if you could clarify on your '25 guidance, what MA margin is implied in that? Thanks.

Susan Diamond - Humana Inc - CFO

Yes, so George, do you want to take the Stars question and then I can take the MA margin question?

George Renaudin - Humana Inc - President - Insurance

Sure. Hi. Thank you for the question, Sarah. So, as we think about the crosswalk possibility, we'll be evaluating that in line with lots of other things. So we certainly want to de-risk the amount of members that we have concentrating certain contracts, and we'll be thinking through that as we go into the next bid cycle.

And one of the considerations will, of course, be how much progress we're making in the current Stars work that we're doing, as well as thinking about the opportunities that we have for crosswalk, the opportunities that we've talked about before with regard to our group contracts.

So there are a number of considerations we'll be taking into hand when we do that, as well as what our '25 membership looks like and membership mix and the progress that we're seeing in medical cost management, some other items. So it is certainly one of the levers we'll be exploring, but I don't think that it is the sole by any means. There are a number of issues we'll be thinking about as we go through -- thinking about our Stars mitigation efforts as we go into next year.

Susan Diamond - Humana Inc - CFO

Yes, and then Sarah, as far as '25 MA margins, obviously, we haven't given any specific guidance yet. Jim provided some commentary, so I'll just remind you. As we previously have talked about our '25 margin expectations on the MA side, we acknowledge them as -- because of the pressures that we were absorbing within '25, including the higher trend that emerged after filing of our 24 bids, V28, IRA, et cetera, and given the TBC threshold, there was limited ability to take true margin expansion within the pricing because the TBC would offset all of those headwinds I just mentioned.

So we had mentioned the majority of the margin progression we would be achieving would largely come from the plan exits where we had exited plans that were historically performing unprofitably, and we didn't feel like we had a reasonable pathway to getting them to profitable or contributing performance levels. That continues to be the case. Again, all of the emerging trend that we've seen, we continue to still feel good about those pricing decisions and how we thought about trends in the aggregate.

As Jim mentioned this morning, though, we are now contemplating some additional investments. The pricing action we took allowed us some flexibility to do that. And so as we've established the notion of a floor, obviously, if we end up closer to flat, the margin will be relatively comparable.

But ultimately, we'll have to evaluate again how membership growth comes in, what levels of investments we do choose to make, and a variety of other things as we set guidance and certainly when we do can talk more about the inherent margin within our guide.

Operator

Joshua Raskin, Nephron Research.

Joshua Raskin - Nephron Research LLC - Analyst

Hi, thanks. Good morning. Do you have a view on MA market growth in total for 2025? And then where do you think the lives that you're losing from those exits are going? Is that sort of one or two larger plans? Do you think smaller plans -- or are people going -- seniors going back to fee-for-service? And I think you just answered this, Susan, but we should assume that those lost lives have lower margins. But does that mean they have lower benefit levels, less rebates? And then lastly, how are you thinking about retention outside of the market exits?

George Renaudin - Humana Inc - President - Insurance

Hi, Josh, so it's George Renaudin. I'll take the question. So on the overall industry growth, we're thinking 5% to 5.5% in this coming year versus the roughly 6% the industry saw this year in our 5% performance that we are expecting as we finish out the year. So we feel pretty good about where that growth is going to come from. And if we think about our competitive positioning, it is very much aligned with our thinking at time of bids.

We continue to anticipate, as Susan said, a few hundred thousand members in 2025 down, so we feel pretty good about that. From a standpoint of retention, there's a lot of work that we're doing to focus on that. We're helping our brokers. As you think about the county and plan exits, there's, of course, going to be a lot of shopping. And so we have put in place lots of tools to help those -- the sales teams, both our internal sales and outside brokers, work through the shopping experience, make sure it's a better consumer experience for our customers.

And so we put in place things that allow the more real-time access and benefits; help them with a best-fit tool, so they can choose the plan that best fits their needs better. And we have also put in place, with our internal team, capabilities including AI to help them with helping those members make better decisions into the needs of the [customers].

I would just say that on another item in retention that we're seeing some very positive results from -- and I think, in the opening comments, Jim made a comment about this, and that's -- that we are getting a better focus into our digital sales, and our new digital sales tool also is allowing us to handle members who were trying to find out as we did do some of those exits. Because, keep in mind, 98% of our members in those exit areas have another plan choice. So the digital tool is helping them make those choices easily, and we're seeing a very significant increase in the amount of digital sales we're having. As a result, all that will lead to increased retention.

Susan Diamond - Humana Inc - CFO

And then Josh, one thing I'd add to George's comments on growth, one thing to keep in mind is we do believe that '25 growth for the industry will still have some impact from the ongoing redetermination process on the MA side. We think it's probably worth about 80 basis points. We're given a deeming period. We will continue to see some attrition in the duals in particular as they lose eligibility.

In terms of your question about how to think about the contribution of lost lives, I would say it depends. As we've always said, for the members impacted by plan exits, those are unprofitable. So to the degree we don't retain them, that is positive. To the degree we do retain them, as George mentioned, because most of them have other plan options, that is incrementally positive because the plans that are available would be positively contributing.

Across the rest of the book, if you remember, we did work very hard and intentionally to make sure we tried to protect our higher-performing plans as we did our 25 bids, so it would have taken less benefit action in those higher-performing plans. And where you'd see larger cuts is going to be those that were below our targeted margin.

So our hope would be that within the attrition that we see, it is more concentrated within the lower performing plans. But obviously, we'll have to see how the AEP results come out. As you know, it takes longer to see the attrition information because a beneficiary has to enroll in another plan. CMS has to process it and give it to us. So we have no real visibility into that just yet but something we'll be watching closely.

Operator

Stephen Baxter, Wells Fargo.

Stephen Baxter - *Wells Fargo Securities, LLC - Analyst*

Hi, thanks. You mentioned that the inpatient unit costs of Medicare came in better than expected. Could you just talk a little bit about what you saw with two midnight rules in the quarter and then just maybe more broadly how you think about the ability of the 2025 commentary to tolerate a higher level of inpatient unit costs in 2025? Thank you.

Susan Diamond - *Humana Inc - CFO*

Hi, Steven. Yes, so you might recall, we've been talking about seeing lower inpatient unit costs really over the course of the year. And I'd say the team in retrospect has just been somewhat cautious and fully stepping up to that. And so we see further runouts to make sure that what we were seeing was durable and would continue.

And that has proven to be relatively consistent; meaning, if we had fully stepped up to what we were seeing early, what we're ultimately seeing emerge continue to be consistent with that. We feel good about what we're seeing. I'd say within the third quarter itself, we start to see some of the flu and respiratory seasonality, which also tends to be lower average unit costs, which would be included in that as well.

In terms of '25, as we've always said, the way we've approached '25 is we've incorporated all of the impacts that got into our '24 baseline. With the changes we've seen across the geography, the lower inpatient unit costs, higher non-inpatient, that is all now embedded into our thinking as a jumping-off point for 25. And then we've got the normal trend as seen for '25.

We now have final rate changes from CMS for reimbursement. And so that obviously is included in our estimates. And so really, what we'd be exposed to is any mix changes. But I'd say based on what we've seen and the consistency of what we've seen, we feel good about how we're thinking about unit cost trends into 2025.

Operator

Joanna Gajuk, Bank of America.

Joanna Gajuk - *BofA Securities Inc. - Analyst*

Hi, good morning. Thanks so much for taking the question. I guess a similar question to Steve's question, but I guess from a different angle. So instead of talking about unit costs, can we talk about utilization trends? Because we've obviously been hearing from some of the hospital companies or the publicly traded companies guiding for volume growth still above average, again in '25 after they are growing well above average this year in terms of just volumes, not just cost.

So kind of the question for you is, just curious, what do you currently assume in your 2025 outlook when it comes to utilization? And then can you grow EPS in that scenario, that this is happening based on that pricing assumption? Thank you.

Susan Diamond - Humana Inc - CFO

Hi, Joanna. Yes, so in terms of utilization, we have seen results that are very much in line from a utilization standpoint since we updated our estimates as of the second-quarter call. At that time, you might remember, we did step up our utilization assumptions and lower non-inpatient just based on what we were seeing in terms of some additional sort of site of service shift related to the Two Midnight Rule.

Our utilization has been very much in line with that since. Obviously, you've got things like respiratory season, the hurricane impact, those things that we can discreetly identify, but our core utilization, we continue to feel good about. Our utilization management impacts have been very consistent coming out of really the first quarter as well, so we feel good about those trends.

In terms of '25, we have the same normal sort of utilization trend on top of that higher '24 baseline that is inherent within our bid. And so again, there's no large incremental regulatory change expected for 2025 that should create this level of uncertainty like we were dealing with for '24. So I think we feel very good about the assumptions we're making in terms of secular sort of utilization trend.

Operator

George Hill, Deutsche Bank.

George Hill - Deutsche Bank Securities, Inc. - Analyst

Yes, good morning. A little bit of a different topic. Can you guys talk about inpatient claims denial rates and how they've trended over the last 12 months? I know in the second quarter, claims appeals was a topic that came up at the margin, and a lot of the publicly traded hospital companies and private hospital companies have talked about an increase in claims denial rates. So I'm just trying to see if there's any meaningful trend to call out there and whether or not claims denials have impacted MLR in any meaningful way.

Susan Diamond - Humana Inc - CFO

Hey, George. Yes, so with the Two Midnight Rule implementation, as we've been saying, that resulted in more initial approval. So in theory, you would expect fewer denials, fewer appeals. As we mentioned throughout the year, when Two Midnight Rule was implemented, we did see initially higher appeal rates and higher uphold rates for those appeals than we would have expected based on historical performance.

As we've mentioned, we've completed audits ourselves. We've been through a CMS audit, which has validated that we believe we're appropriately evaluating the clinical rules. And what we would say is, at the time, there was a question about, was that just a pull forward and a change in seasonality of how appeals would come in? And would we see fewer appeals in the future? Because there's a reasonably long tail over which providers can appeal.

We made the assumption that it would just result in overall higher appeals and ultimately uphold rates. That is what we have been seeing to date. We would just say we caught that early and incorporated into our estimates coming out of the first quarter. I think why you may be hearing some different commentary from hospital systems is they may not have recognized that as quickly and may have seen that higher appeal rate initially and assumed that the absolute appeals would still be comparable year over year.

And what we've just seen is those appeals have been higher, which, when you think about just the magnitude of the changes, I think it's everybody just trying to understand how those new rules are being applied across the payers and then the providers. So that's, I would say, very consistent with what we've seen since the first quarter and no meaningful variation since.

And then, George, I don't know if you want to add anything?

George Renaudin - Humana Inc - President - Insurance

Yes, I would just add that I think you're right about the question of testing the appeals and seeing where they aren't trying to figure out exactly how the two-midnight rule will be applied. We, as you said, feel very confident about how we're applying it given the CMS audit we had the very start of the year that came out positively.

The other thing I would just add to that is that our clinicians continue to speak with many of the provider clinicians to talk through the issues to make sure we all have a similar way of approaching that everyone is clear and understanding what the two-midnight rule is and is not.

Jim Rehtin - Humana Inc - President, CEO, & Director

Hey, not to pile on here, but let me just try to wrap all the inpatient stuff together. Broadly, I think what we're trying to convey is that since late first quarter, early second quarter, we've seen relatively stable trends. And so there was a fair amount of noise in the first quarter. I think everybody was adapting to the regulatory change.

For us, we put a lot of attention on it at that point in time. And we think we worked through all the changes in process and approach and whatnot and have gotten to a relatively stable place. So when we look forward, we're feeling pretty good about the outlook and our ability to project what the inpatient cost is going to be, whether that's denial rates, utilization, unit cost, et cetera, relative to where we were back in the first quarter.

Operator

Whit Mayo, Leerink Partners.

Whit Mayo - Leerink Partners LLC - Analyst

Hey, good morning. Maybe just a question on Stars as it relates to the lawsuit or appeal, just looking at each contract, 5216, maybe the math is off a little bit here. But it seems like you might need to flip both the Part C and D ratings on the call center to a 5 from a 4 to get back to a 4-star rating on that contract. It doesn't seem like you can do it with just improvement in one category. It seems like both. So is that an accurate statement? And I'm just wondering, how many calls ballpark are we talking about to have to overturn to see improvement in either category? Is it one? Is it multiple calls? Just any color would be helpful, thanks.

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, in total, it's three calls across both metrics. And yes, we would need to see the three calls overturned.

George Renaudin - Humana Inc - President - Insurance

I would just add into that, Jim, that in addition to the three calls, one of the other things that we're talking -- that we are pursuing with CMS is the need for greater visibility and transparency into how the thresholds are calculated.

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, that is correct. Yes.

Operator

A.J. Rice, UBS.

A.J. Rice - UBS Securities LLC - Analyst

Hi, everybody. Just want to make sure I understand the early thinking on '25. If you are successful in your appeal on the Stars through litigation, would that change your view on the amount of investment you need in '25? It almost sounds like up to this point, the discussion around the Star ratings hit has been around the arbitrariness of the CMS threshold cut points and some of that, and you've had a great track record of having very high Star ratings.

Now all of a sudden, it sounds like, as you guys have looked at this, you now think you need to make a lot of investment to get back on track on Stars. And I wonder, if your appeal is successful, would you not have to do that? And would that change your outlook for '25 for the better?

And then, in the broad discussion about out years, there's always the discussion about trading off enrollment for margin. And obviously, we've got a lot of focus on getting you back to 3% margin, but any philosophical commentary about how much of an enrollment hit you might end up taking if the appeal is unsuccessful to get back to that 3% margin over the next couple of years with a view to '27?

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, so let me start with the appeal and its impact on how we think about 2025. So the way to think about Stars is there's two related but slightly different things. So there's the appeal related to the single -- or I guess two but similar metrics that are kind of the difference between 3.5 and 4 stars for a whole bunch of our members. That is one thing that is working its way through litigation. We're not really going to comment on that beyond what we have.

But separate is the broader trend within the Stars program of cut points and thresholds getting harder. And that's across a lot of different metrics. And so while there's one critical metric for BY 2026, broadly, I think the entire industry is looking at a movement in metrics and cut points and thresholds that is causing pretty much everybody to reevaluate how far do you have to lean into investment in this program to make sure that you can keep up with that metric movement. I don't think we're alone in that.

So as we contemplate investments for next year, the appeal is not going to have any kind of meaningful impact on how we think about investment. The investment is going broadly in the program to drive better and better and better performance at a pace that exceeds what we expected previously. That's really what the investment is about at the end of the day.

George, would you -- anything you can add to that?

George Renaudin - Humana Inc - President - Insurance

I would just add, Jim, that the other thing about the investments we're making in Stars are, in many ways, the right thing to do to improve health outcomes for our members overall. The investments we're making are enhancing our provider member performance. We're talking about incentive programs to close gaps in care, which helps our health outcomes, while also improving the customer experience.

It is a good thing for us to continue to work with our vendors to improve our relations with them and to improve their performance. And finally, the strengthening that we're doing around technology and integration to support operational excellence also nicely folds into many of the other things that Jim has talked about we need to focus on moving forward in both his opening comments and in his earlier letter.

Susan Diamond - Humana Inc - CFO

Yes, and then, AJ, the only other thing I'd remind you is we talked about investments for 2025. Just keep in mind, Stars is one piece of it, but there are investments we're making more broadly to drive just improved operational performance across a number of areas that Jim had referred to, so Stars is just one component. And then, Jim, the last question I don't think we touched on is just the philosophy of membership growth and margin trade-off, if you wanted to touch on that.

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, and again, I think this was related to how would we react to the Stars mitigation or Stars progression. Look, the short answer is we have a lot of questions around that very thing that we're going to have to answer over the next three, four, five months. So we don't have a perfect answer.

We've got to understand, what does the rate environment look like? How are we feeling about the progress that we're making on 2027 Stars, et cetera? So there's just a bunch of factors that we don't yet have visibility into to answer that. What I would say, just generically, is our intent is to balance long-term earnings potential with near-term earnings progression. We need to balance those. All in all, we're not going to do things that harm the business long term to work our way through a short-term issue. Now what does that mean practically? We don't know yet. We have to sort that out.

Operator

David Windley, Jefferies.

David Windley - Jefferies Financial Group Inc. - Analyst

Hi, good morning. Thanks for taking my questions. I wondered on two fronts. First, on channel investment, basically, you've touched on some of this already. I recall last year that after AEP, the discussion was that the brokers were more consumed by helping existing members shop and therefore couldn't talk to new members as much, resulting in AEP growth being relatively low, more shopping expected for 2025.

I'm wondering what you've done to address that issue. And kind of relatedly, how should we think about the cadence of membership AEP versus entry year? And then lastly, I'm wondering just if you have any early thoughts or expectations about '26 rates for early next-year announcement. Thanks.

George Renaudin - Humana Inc - President - Insurance

Yes, so I'll start, and there are a number of -- thanks for the question, David. There are a number of things that we've done in preparation for what we knew was going to be a sales year where there's going to be a dynamic change in the industry given the industry reset that we've all talked about we're going through with benefit changes, member disruption, as we have had planned in-county exits, a number of our competitors have as well, so we know that that's going to be something that we have to focus on.

So we continue to make investments in both our internal sales channels to include improvements in, as I mentioned before, digital self-service options. We also are making investments to help our external brokers. You also realize that we have a pretty large internal brokerage as well, and we're seeing a 70% increase in sales in that internal brokerage channel.

So we're going at this from both improving the experience for the members to be able to self-service in digital, improving when our sales team gets those calls in person, how they can answer those questions by giving them better tools and leveraging AI, as well as helping our external partners in providing them with more real-time data information and helping them on best benefit choices. So there's a whole host of things we're doing across the whole marketplace that we are prepared for, knowing that this is going to be a year of pretty significant change in this AEP.

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, and let me just kind of headline that our external partners are really important to us and building and strengthening our internal channel is what we have the most direct control over and we've been building capacity in that internal channel for that very reason. And that channel is also very important to us. And so we have built capacity to the degree that we feel like we reasonably can under the timeframe and the circumstances, et cetera. And at the end of the day, we still look at the market and we expect 5% to 5.5% growth at the end of the day, even with the need to kind of balance these capacity constraints.

Susan Diamond - Humana Inc - CFO

And then I think the last question was around 2026 rates, which, David, I would just say it's hard to -- we can't really predict what it's going to be. We would say we still have V28 and IME to be saved in, so we know those are impacts. And the big question will be, given the trend that we have seen, will we see some positive restatement embedded within the '26 rate?

Recognizing their forward-looking '25 rate, it is seeing some trend improvement, which obviously hasn't transpired. The ACO reach detail that's shared by CMS is one sort of indicator of the trend they may be seeing. That does suggest that they are seeing some of these higher trends as well. So I think we're cautiously optimistic that the rates for next year will include an appropriate adjustment for the trend that we're all absorbing.

Operator

Michael Ha, Baird.

Michael Ha - Robert W. Baird & Co. Inc. - Analyst

Hi, thank you. So just firstly, quickly to confirm, on DSNP redetermination, Susan, did you mention 80 bps of industry growth has been expected for next year? Is that presumably because of the six-month grace period they have? Are the bulk of those lives still yet to be determined -- redetermined? What percent of those lives are expected to fall off your book?

And then number two, I guess, given that you're already 11 months into the measurement year, '24 for next October's release, Star ratings, I know CAHPS still runs through June. But based on the other, I guess, let's call it roughly 70% waiving -- or actually, I guess 80% now that CAHPS is being reduced. I know you're in a sprint right now, but how are you tracking on those 80% of measures?

More specifically, I guess what's the realistic likelihood of being able to sort of fully snap back to 80% to 90% of members and 4-star plus plans? What's your level of confidence, conviction? Or is it just very unlikely given how late into 2024 it is and how late it was, realizing how aggressive cut points are, and just the time you have left to make incremental improvements. Thank you.

Susan Diamond - Humana Inc - CFO

Sure, Michael. I'll take the first question, then hand it over to Jim or George for the Star question. On D-SNPs, yes, you heard that correctly. We do anticipate a headwind in 2025 as the re-determination process completes. There was pressure in 2024 as well, slightly less than, we would say, 70 or so basis points in 2024. And we think it will be about 80 basis points of pressure in 2025.

Frankly, part of that is because of the Change Healthcare disruption, which disrupted the ability to confirm eligibility. And so even though we've largely seen the impact on the Medicaid side, because of the deeming period, on the MA side, there is that six-month period. And so we do expect that we will see some additional dual disenrollment as they lose coverage.

Some of those we would expect to recapture within our non-D-SNP offerings, but some, obviously, are no longer eligible. So we've built that into our expectations all along for '25 in terms of the loss of a few hundred thousand members that is already contemplated. But yes, you did hear me correctly.

And then George or Jim, do you want to take the Star question?

Jim Rehtin - Humana Inc - President, CEO, & Director

Yes, I'll just jump in on that. The short answer is, at this point, one, you've just got limited visibility into even your own performance, and you've got no visibility into industry performance. And so we're not going to comment on industry performance or cut points or thresholds until they're actually out next year.

On our own performance, we feel good about the progress that we are making. And there is risk. We're resetting expectations with four months, 3.5 months to go in the year, setting those expectations higher, driving towards higher goals.

And while I think we all feel good that we are making progress and leaning as an organization into it as heavily as we can, we still need time to understand exactly how those things are going to play out. So there's just -- there's not a super clear answer to the question at this point in time. But everybody is leaning into it, and that is what we need right now.

With that being the last question, I'm just going to transition here and thank everybody for joining us this morning and thank everybody for your interest in Humana and in what we are trying to do to serve our patients and our members. And I want to thank our 65,000 associates who serve those members and those patients every day. We appreciate the work that they're doing, and we appreciate the support that you're giving us, so thank you.

Operator

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

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