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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 First Quarter 2024 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 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, both of which are available on our website. We will begin this morning with brief remarks from Bruce Broussard, Humana's Chief Executive Officer; and Jim Rechtin, Humana's President and Chief Operating Officer.

Followed by a Q&A session, where Bruce and Jim will be joined by Susan Diamond, Humana's Chief Financial 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 first 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 and 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 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. I hope you had the opportunity to review our prepared remarks, which we posted this morning along with our earnings release. We'll spend the majority of our time today on Q&A, but I'd first like to highlight a few key messages that we want you to take away from our discussion.

First, we had a solid start to 2024 and we're pleased to reaffirm our full year adjusted EPS guidance of approximately $16 while increasing our individual MA membership growth outlook by 50,000 to 150,000 net growth. Early medical cost trend indicators in our individual MA business are largely in line to positive relative to expectations, and we have seen strong year-to-date patient growth in our primary care business with 20% growth in our de novo centers and 7% growth in our more mature wholly owned centers.

In addition, we are incredibly proud of our continued organic success expanding our Medicaid platform with recent contract wins in Florida, Texas and Virginia. We are pleased that 2024 is trending in line with expectations. As we look ahead, we acknowledge that the industry is experiencing a dynamic and challenging time we must navigate. And while the current environment will create disruption for the industry in the near term, we continue to believe in the strong core fundamentals and growth outlook of the MA industry and our ability to effectively compete in MA market remains intact.

Specific to 2025, we expect benefit levels, planned stability and choice for seniors to be negatively impacted by the final MA rate notice, which is not sufficient to address their current medical cost trend environment and regulatory changes. Considering the significant difference between the final rate notice and our previous funding assumption, combined with the inherent pricing limitations imposed by the TBC change thresholds, we no longer believe $6 to $10 of adjusted EPS growth is the appropriate target range for 2025.

Importantly, we believe that the industry will adjust to the current funding regulatory over time, continuing to deliver strong top line growth and normalizing at an appropriate margin of at least 3%. In that context, we remain committed to margin recovery and profitable growth through a multiyear pricing actions, creating value for our shareholders over the long term.

Our 2025 adjusted EPS growth outlook will be impacted by several variables to which we will not have clear visibility until later this year, including finalization of our MA bid pricing decisions, the continued evolution of the industry cost trends, and the level of competitor pricing actions in 2025, which will impact our net membership growth.

In addition, we continue to evaluate opportunities to drive growth and further productivity across all lines of business to support 2025 adjusted EPS growth. We appreciate your desire for more detail regarding our outlook for 2025, and we will, therefore, provide an update on our bid strategy post bid finalization, with further update in the fall once we have visibility into our competitor plans and expected membership implications.

Before turning it to Jim for a few remarks, I'd further emphasize that we continue to believe there is strong bipartisan support for the MA program and that the strong core fundamentals and growth outlook for MA and value-based care remain intact.

In addition, Humana's platform, unique focus on MA, and expanding CenterWell capabilities will allow us to compete effectively and deliver compelling shareholder value over the long term.

With that, turn it over to Jim.

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

Thanks, Bruce. I just want to echo your comments that the outlook for Humana specifically and for the MA industry more broadly remains strong. The industry is navigating a challenging time, but it's important to recall that this is not the first time that we've had to navigate challenging times and that we've seen difficult periods in the past. Humana has navigated this period successfully adjusting as needed and continuing to grow.

While we anticipate disruption in the near term, the sector fundamentals are sound. This includes favorable demographics, a compelling value proposition relative to traditional Medicare. We believe the industry will continue to grow, and Humana will be well positioned to remain a leader in the market.

I also want to reiterate that we are committed to pricing discipline and margin recovery in this bid cycle. We are actively evaluating plan level pricing decisions and the expected impact to membership. We are evaluating opportunities to drive productivity, we are focused on the levers to support adjusted EPS growth in 2025 and beyond. And as we have incremental data on 2025, we will share it.

We appreciate everyone's ongoing support and look forward to providing additional updates, our performance and outlook throughout the year.

With that, we will open the line for your questions. In fairness to those waiting in the queue, we ask that you limit yourself to one question. Operator, please introduce the first caller.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from the line of Ann Hynes with Mizuho.

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

I just want to focus on cost trends. Did you see any change in cost trends versus 4Q? Also in your prepared remarks, it sounds like the company believes they took a conservative approach to reserving just given the Change Healthcare situation. Can you suggest that early indicators suggest trends were in line or better. Can you just elaborate on that comment, that would be great.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. This is Susan. So as we evaluate the first quarter cost trends, as you guys understand, we do have good visibility to inpatient utilization from their more real-time authorization data. On unit cost and non inpatient, we are more dependent on claims. And so typically, in the first quarter, have limited visibility and given the Change Healthcare disruption even more so this quarter. .

But as you might remember from our fourth quarter commentary, one of the things we did experience was an unexpected uptick in inpatient utilization, which we did believe was in some way related to the expected 2-midnight rule changes that went into effect in January. As we said in our fourth quarter, we anticipated that those higher utilization levels would continue into the first quarter and then be further impacted by the changes we had always anticipated in response to the changes to utilization management programs.

So as we evaluated the first quarter inpatient utilization, I had provided some commentary a couple of weeks ago at a conference and acknowledged it. For January and February, we did see slightly higher inpatient utilization, where the ultimate impact of some of those program changes was a little bit different than we had expected, but we had commented that the results were improving week to week.

We continue to see that, such that, while we were exiting February, we would say that the last week of February results were much more in line and we saw that continue into March and even some slight positive favorability such that for the full first quarter, as we said in our posted commentary, inpatient utilization overall is in line with expectations. So that's positive.

We'll have to see how the non-inpatient trends and inpatient unit costs develop as we get more visibility into the claim maturation.

The other early indicator is how prior year development matures. In the first quarter, we feel like we have better visibility for incurred claims through the third quarter of 2023. We think that the Change Healthcare disruption was more impactful to incurred periods of the fourth quarter and more recent. So we felt comfortable relying on what we saw through the third quarter.

And as we said in our commentary, we did see positive favorable -- positive prior year development, particularly for the third quarter across both inpatient and non-inpatient. So we view that as positive.

As the claims further mature, our hope is that we'll see some further [progress] into the fourth quarter. But for purposes, our quarter-end reserving, we did not contemplate that just because we recognized we have limited visibility.

As you said, as we did our analysis for the first quarter, we made an explicit adjustment for what claims we believe were missing due to the Change Healthcare disruption. And just based on those results, we would have seen some net positivity in the quarter all in. Because we did recognize that we didn't have full visibility, we did go ahead and book additional claim reserves that ultimately reported our MLRs in line with expectations.

So our hope is that we will see that, that proves to have some conservatism. We will see how that continues to develop as all of those claims are received and processed, and we'll keep you guys updated on any intra-year development. But otherwise, hopefully, that's helpful in understanding what's reflected in the first quarter.

Operator

Our next question will come from the line of Kevin Fischbeck with Bank of America.

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

I wanted to just maybe focus on the commentary around the 3% plus margin, which seem to be orienting towards kind of the lower end of the 3% to 5% margin than many of your peers are talking about and maybe a little bit lower than what you were talking about before. Is that -- if that's true, then why would that be the case for you guys? And then I guess over the last couple of years, you've been trying to reorient this towards an enterprise margin. I would love to just kind of hear how you think a 3% MA margin translate into what the implied enterprise margin might look like.

Susan Marie Diamond - *Humana Inc. - CFO*

Kevin, yes. So yes, we continue to be oriented to enterprise margin and maximizing that across the health plan and CenterWell capabilities. And so don't intend on a recurring basis to speak specifically to the health plan. But given the magnitude of the impact we're anticipating for 2023 and 2024 and our acknowledgment that the margins currently are sitting closer to breakeven, we felt it was important to reiterate our view of what the long-term margin potential should be minimally for individual MA, not only for Humana, but the sector more broadly. And we do believe that 3% plus is a reasonable margin longer term.

Now to the degree the industry ultimately normalizes to something higher than that, we're not trying to suggest we would intentionally suppress it. We would expect to have a margin on par with the industry and competitive, and we think that would be minimally 3%.

I would say, as we think about the CenterWell opportunity, as we've said before, there's literal incremental opportunity from just further penetrating our CenterWell capabilities by health plan members, which we continue to focus on.

And then in addition to that, we do believe over time, if we can create differentiated experiences for our members who use those services, then we can increase claim satisfaction, and patient satisfaction, increase engagement, which should ultimately lead to better service results, improved loyalty and retention and overall improved total cost of care health outcomes, which can be driving further incremental margin and also reinvest it back in the business to support further growth.

So we remain as optimistic as ever about the long-term potential and do just acknowledge in light of the final rate notice our progression back to that minimum 3% health plan margin will take a little bit longer than we had initially expected.

Operator

Our next question will come from the line of Gary Taylor with TD Cowen.

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

Two quick things I just want to make sure I understand. Back on the first quarter call, we asked about TBC and you felt it wasn't a constraint to margin recovery for '25. And I think what's changed is that might have been true with the 0% funding assumption, but at a negative [1 6] you're just more underwater, so to speak, from an underwriting perspective. And so now TBC is more relevant to '25. So I just want to confirm that.

And then secondly, that $6 to $10 bridge, in our view, the final notice, on paper, wipes out most of that bridge. But at our conference in March, you had suggested you had still expected to see some earnings growth for '25. So I just wanted to see if you could affirm that expectation today?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. Gary, and you are correct. With where the final rate notice came in, it will require larger benefit reductions to achieve stable margins and approach the TBC thresholds in some cases. And so that's where, as we said all along, we will be evaluating plan and county exits where the TBC limits impede our ability to price products at a reasonable margin.

And then also look for opportunities within the bids to optimize benefit changes, to support further margin improvement. Given the competitive bidding process, we're going to avoid sharing any specific details today on what that might look like. But certainly, as Jim suggested, post bid, we'll be able to share a little bit more detail on how we approach the strategy for '25 plan designs.

We do recognize that in light of the final rate notice sort of net membership will be more impactful to what we can ultimately deliver for '25 earnings than it might have been in the previous thinking. And so that's where we just feel like we need to have more visibility into competitor reactions to the final rate notice before we can really evaluate that.

The final thing I'll say is, technically, as we sit here today, we do not have the TBC threshold for 2025. And so to the degree that moves even a couple of dollars positively or negatively, can impact ultimately what we think we can deliver for margin progression given where we are. So for all of those reasons, we're just going to need some additional time. But as we said, as we know more, we will make sure to update you and provide you with information as we become more confident in the information that we have access to.

Operator

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

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

Hello, can you hear me?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes.

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

So one, I wanted to follow up on Kevin's question and then I got one of my own. The 3% margin, the 3% plus target, my recollection is when I did the math for 2025, when you originally had the $37, I was getting to about a 3.5% individual MA margin within that $37. Is that the right ballpark that you'd previously assumed just so we can compare or contrast?

And then can you confirm that this doesn't include investment income, which I think makes them a little less comparable? And then my question is on 2025. At this point, rates are known and the key -- I know TBC is still got to come. You've got to make some decisions. But the key swing factor appears to be Medicare Advantage membership. Get that there's less visibility here, but maybe you can walk us through. I know I get a lot of questions on the P&L impact from lost membership, right? I'm thinking specifically beyond the loss margin, deleveraging on SG&A, whether you can offset that with efficiencies. And then any kind of downstream impacts from CenterWell. So maybe you could give us a framework to think about like every 1% decline in membership, the negative impact through the P&L ex the loss margin might be ex something.

Susan Marie Diamond - *Humana Inc. - CFO*

Okay. Yes. So I think that was 6 questions in 1, but I will do my best to hit them all. To your first comment about the $37, you are correct. And here in that initial modeling, you can think of it between 3% and 3.5% over that period. And we had always said that our belief was that any margin progression and improvement would largely come from productivity and efficiency, not MLR gains and then any sort of revenue and claim trend vendors would sort of support the product to remain competitive and continue to grow.

But, yes, you were correct in terms of where we would have been thinking in the previous guidance. And you are correct, the 3% plus that we referenced does not include investment income. And so that can sometimes vary in terms of how peers report their margin targets. But for us, that would exclude investment income.

In terms of '25, as you said, TBC is going to be a huge factor, just given where we think we are in terms of expected benefit changes and the net membership growth, as you said. The other thing I'll mention before coming back to membership is just trend. Depending on how the trend develops in, well, frankly, how '23 ultimately restates, how '24 develops, that could be impactful to '25 as well.

We are not pricing for any favorability to emerge in 2024. And so to the degree it does, that would be incrementally positive going into next year as well. When you think about the membership, I would say the absolute membership is certainly important. And in light of the final rate notice and the expected changes that we expect, we think our ultimate result will be more sensitive to the net membership than it might otherwise have been.

And then in addition to that, I would say, plan mix underneath. There are varying margin profiles across a deal versus non, certain geographies and other factors. And so that mix ultimately will be important and how our plans are ultimately positioned relative to others.

I would say right now, as we've said all along, we are anticipating that membership declined for 2025, largely because we do intend to exit certain plans in counties whether that is incrementally larger or smaller based on the other plans will be very dependent on what we see across the competitive landscape. And as we know more, we'll certainly keep you apprised of our thinking.

Depending on the level of membership change, we certainly will be mindful of driving the appropriate admin cost adjustments in light of that. We are currently, as I said, planning for membership losses, so we would be proactively anticipating that. The variable is certainly much easier to address than normal course. We would just have to be very mindful of the targets we set across some of the nonvariable items, but certainly are anticipating that and we'll have strategies in place, should you see differences in the membership that we're currently thinking.

And then finally, I would say, generally speaking, the largest CenterWell business that's impacted by any net members to change is the pharmacy just given the penetration within the Humana pharmacy. That also is fairly sensitive to mix, less sensitive to dual changes who use mail order at a lower rate and be more highly sensitive to consumers who were shopping on value in terms of those co-pays. So that's something we'll continue to monitor. But I would say mostly, we would be looking at the impact of pharmacy. But impact will be much smaller across primary care and home and primary care, in particular, because they continue to have work on contracts with other providers such that even if we see a member just on a health plan side, hopefully, they're positioned to retain them on the clinic side through their other payer contracts.

Operator

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

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

Just to clarify the TBC commentary, our understanding is there are a lot of benefits that are not governed by TBC like flex cards. And it seems like you're suggesting that you're not comfortable making up the incremental rate headwind by cutting benefits that are outside of TBC. I was hoping you could elaborate a little bit on this dynamic and how you're thinking about the sensitivity of benefits that are outside of TBC thresholds.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. Sure, Stephen. So I would say on the non-D-SNP side, as we talk about the [benefits], most of the benefits are [submitted] to TBC. So even things that are technically supplemental things like dental, Part B givebacks and for those are for purposes of TBC accounting tools. There are some items that fall outside of TBC, some things like transportation, OTC, fitness and a few other things, but are relatively small versus those things [due to product] TBC.

We will be considering changes across both categories. Certainly, and in some cases, we will be going above TBC. In other cases, not. And that will be -- as we evaluate just the current financial performance of the plan. Even post some of these impacts and whether we believe it's situated in a way that can drive profitable growth in a sustainable way. For those plans, as we said, that are not, we will go to the maximum that we can in order to ensure that the products are properly positioned.

On the D-SNP side, technically, they don't apply TBC to the D-SNPs and most of those benefits are going to be the supplements, right? You've got the healthy options card because it covers food, OTC, transportation. So technically, there is no limitation on that side. And so that is more thinking through how are those plans financially performing, what's the opportunity for further growth in those markets. Those are all things we will be considering. We do expect benefit changes on the D-SNP side. And the dual plans will see more impact from the IRA as well. So those are all things we'll consider, but technically don't have the same literal TBC limitation.

Operator

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

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

I was wondering if you could provide a little bit more information on a previous utilization question. You mentioned earlier some measures you took to address the higher mix of short-stay inpatient volume versus observation stays. You saw earlier in the year, and I believe you've noted some training and other measures to bring those inpatient avoidance rates back in line. But just curious to what degree those measures impacted your APT performance for the quarter. And if there could be, that could be a source of some outperformance through the balance of the year versus your 90% [MER] guidance.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, Ben. So you are correct. So as we said on our fourth quarter call, we were anticipating in light of the 2-midnight rule changes that we would see an increase in short stays and things that under the old rules were built as an observation, they would now flip to an inpatient's stay. And we saw that in the fourth quarter start to emerge and did continue to see that in the [first] quarter incrementally. .

As we said at the Cowen Conference, initially, we did see the avoidance rates fall short, a bit short of what we had expected. But as we said, as the providers and our staff were sort of trained and became accustomed to the new rules, we did see those rates improve week over week, such that by the time we exited February, they were much more in line with what we expected.

So as I said earlier, we did see some unfavourability in APT's January to lesser degree in February, but then March, as we saw those rates come in line, we're actually slightly positive such that for the full first quarter, largely in line on a utilization basis.

One thing we want to continue to evaluate is what the resulting unit cost is on those higher incremental APTs. In theory, they should be lower. That could provide a tailwind for the year. But as we said before, we're relying on the claims coming in and being paid to fully assess that. So we did not take that into our first quarter results and something that we'll continue to evaluate over the second quarter. But I do think potentially could be a tailwind relative to our expectations.

The only thing I'll say is that, if you think about the 90%, if you remember earlier this year, we did acknowledge that the changes to the physician payments that were implemented in February did present a headwind to our internal plan. And that was worth about $150 million for the year. We did not change our MLR guidance this morning. And so you can assume that, here now we're assuming that we will cover the impact of that physician fee schedule change.

And so some of this positivity would certainly help do that. But if for some reason, we didn't see that emerge, obviously, with the admin cost favorability that we delivered in the first quarter, we certainly have confidence that in any event, we'd be able to cover it through admin savings. But as we said in the commentary, cautiously optimistic about what we're seeing on the individual MA side. We'll just need to be able to further evaluate paid claims from both the unit cost perspective and the non-inpatient trends.

Operator

Our next question will come from the line of A.J. Rice with UBS.

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

Can you hear me?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, A.J.

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

Sorry, just went dark there for a second, so I wasn't 100% sure. Just two things real quick, you had talked about, I think, with the fourth quarter and even some of the year-end commentary that the road to recovery on the margin was about, you thought the market could absorb 100 to 150 basis points of annual improvement over the next few years. Calling beyond that might be disruptive from a competitive standpoint or for seniors and you thought you could get that.

I guess I'm trying to understand, is that -- is this sense about your ability to realize that from year-to-year over the next few years changed? Are you just saying that the '25 starting point might be lower, but you still kind of get that kind of gradual recovery to margin over time? Any perspective on that? And you haven't been asked, but in the press release, you said something about operating expenses having some timing impact in this quarter that might have been favorable. Can you comment on that and how that affects the rest of the year outlook?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, A.J., certainly. So in terms of our thinking on the trajectory to the 3% longer-term expectation, we would say that we do acknowledge this is going to be a multiyear process to recover margins. And the exact timing of that will be dependent on the funding environment, regulatory environment and then certainly the competitive environment.

I would say relative to what we would have thought and prior to the final rate notice coming out, we would have anticipated, as our previous guidance suggested that we would have more margin recovery in '25 then we think is reasonable currently in light of the TBC threshold combined with the final rate notice.

Also keep in mind for '25, we're dealing with not only 1/3 phase-in for V28, but also significant Part D changes from the IRA and then the higher-than-anticipated medical cost trend that largely developed post the filing of the '24 bids. So that is going to limit to some degree the amount of margin recovery we can get in '25.

When we think about '26, while we still have one more -- the final 1/3 of the V28 phase-in, we won't arguably have the Part D changes, we won't have the trend impact. So those headwinds will lessen, which then should give us more room to take additional pricing action for the purposes of margin recovery.

And then certainly, post '26 once V28 is fully phased in and assuming a reasonable rate environment, then we should have further incremental opportunity, which is why we've suggested that it's likely going to take a bit longer than the 2 years we had hoped previously.

The other thing I would just remind you is that to the degree the trend develops different than what CMS assumed in their '25 rate notice, which if you remember, anticipated the trends would actually moderate from the current levels. Then that ultimately should make it into the CMS rates as well and could potentially provide a slight tailwind as you think about the go-forward rate environment. So a lot for us to continue to monitor and assess, but do believe that '26 and beyond provide incremental opportunity for margin recovery relative to '25 for all the reasons I just mentioned.

And then on OpEx, as you said, we did see meaningful favorability for the quarter. As we evaluate that favorability, some of it, we believe, will continue and largely for the year. A portion of that, we would say, is onetime in nature where it's good news, but it's not going to repeat. And then there is a portion that is more timing where just it developed different than we had assumed in the budget. And so things like marketing are often an example of that where it may come in differently, the pacing of hiring may be different.

And so there's a variety of things that we would say are more timing in nature that won't, in fact, not only will not recur, but they'll actually reverse out in the balance of the year. But all in, still positive, we expect favorability for the year. For OpEx, it just wouldn't be appropriate to fully run rate the first quarter.

Operator

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

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

Can you hear me?

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

Yes, Scott.

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

I was interested if you can maybe talk about how you would think about the value prop for seniors, potentially comparing between MA and traditional Medicare in 2025. Obviously, we're all very focused on the headwinds to the MA value prop as it relates to the challenging reimbursement outlook. But it also feels like seniors in traditional Medicare are going to be facing some meaningful headwinds as well when we think about the IRA impacts on Part D.

And then also just in terms of, curious what you've been seeing on utilization in the [MedSup booking] whether that may be leading to higher rate increases in Medicare Supplement. And also just thinking about the fact that CMS talked about not seeing utilization rising in Medicare fee-for-service, which clearly seems to contrast with everything we've seen out in the marketplace. But ultimately, I'm just trying to think about, is there a potential that MA enrollment growth relative to traditional Medicare may not necessarily moderate as much as feared because of some of these headwinds, introductional Medicare or are the headwinds in MA just so significant that it is likely that we'll see that moderation?

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

Scott, thanks. I'm sure Susan is saying thank you, too, to give her the break of all the questions that have been asked relative to the financial side. Relative to the value proposition for Medicare Advantage to MA, we continue to believe we will have a significant value proposition. And really for a number of reasons. First, just the economics itself, I mean, today, we see about $2,400 a year. You see that stepping back a little bit for 2025 as a result of the benefit changes, but not material to make it something that we feel shopping to the Medicare fee-for-service side will increase.

The second thing is that all the benefits that they receive as a result of care coordination, things like transportation, other things like dental that they wouldn't get in a Medicare fee-for-service product. And so we just see not only the dollar value from an actuarial point of view, but also the inherent additional benefits that they receive as a result of being a Medicare Advantage beneficiary. So we see that continuing to be the case.

We've done a significant amount of analysis around where the value proposition is today, where it was 3, 4 years ago. And what we see is that the value proposition still will be greater than it was 3 or 4 years ago, a little lesser than today, but we feel confident that we'll see the growth there. With that, do you want to -- Susan, do you want to take the Medicare supplement question?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. On MedSup, interestingly enough, the Change Healthcare disruption was particularly disruptive to our MedSup business. And so I don't know if that's a function of just CMS not working with providers for redirection versus the MA plans, I'm not sure, but we did see a disproportionate impact to MedSup. And so I would say that our current visibility is a little bit less than it would typically be.

Otherwise, I would say the IRA impacts for 2025 will impact Part D, as you said. And we will see varying degrees of impact across the plan -- the stand-alone Part D plans, just recognizing the underlying mix is different for each of those plans. And so to your point, those who are in MedSup are also having to purchase a stand-alone Part D plan. And so that's certainly should give them a different perspective in terms of as they evaluate the value proposition of MA, and we'll act as a bit of a mitigant in terms of what we see the impact to the MA plan offerings themselves.

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

And Scott, I think your other question was just relative to the growth of Medicare Advantage and just how that looks. And we continue to see and believe over the coming years that it will be a mid-single-digit growth, and that will be a combination of demographic growth, maybe slowing a little bit in the latter years of this decade, but we continue to see that along with the penetration of more beneficiaries using Medicare Advantage.

Kaiser put out an estimate over the next few years that there will be about a 60% penetration with MA and we continue to believe that's very achievable going forward. So we feel the value proposition is going to continue to be strong as a result of not only the actuarial value, but also the additional benefits. We continue to believe that that's going to drive more penetration of Medicare Advantage for Medicare beneficiaries overall. And so we look at continuing to maintain mid- to single-digit growth.

Operator

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

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

Just getting back to the 3%, I guess, how did you come to this long-term industry margin of 3% plus? What does that mean for Humana relative to the industry? And what do you think that translates into in some form of like return on invested capital?

And then just a follow-up on the exits. I'm just curious what percentage of your membership is in areas that are even being considered for market exits. I'm not looking for a specific estimate of how many members you'll lose, but just a sense of how many markets are even in that bucket of consideration?

Susan Marie Diamond - *Humana Inc. - CFO*

Josh, so as we think about the 3%, and as Justin had asked earlier, that even historically had been -- how the business has been performing and expectation that we would be able to continue to maintain that level of performance and believe that the industry will minimally require that level of margin, just recognizing the inherent sort of risk in the insurance business the regulatory capital that has to be established. But that just feels like an appropriate margin on a sustainable basis and certainly reasonable and still be able to provide a very strong value proposition to consumers.

Also, as you look at the long-term targets that most of the national peers have talked to, it is in the 3% to 5% range. And as we said earlier, there are some differences in what's included in those numbers across the peer set. But certainly, everything that we have seen and believe and others, I think, have reiterated is, I believe that the long-term margin is down. We just have some environment to navigate in the near midterm to get back to that and have all of the health plans reflect not only the funding environment, but then the more -- the higher more recent trends that we've experienced.

In terms -- and then I would say, in terms of return on invested capital, because that, again, is similar to what we've historically or more recently performed, I would say no material things that how we would think about the expected returns for the business.

In terms of market exits, again, just given the sensitivity on -- we haven't commented specifically on either number of plans, as you said or percentage of eligible covered and we'd feel more comfortable sharing more information on that post bid filing. And certainly, we're happy to do that as we have in the past and we have executed larger-scale plan exits. Just don't feel comfortable doing that in advance of the bids being submitted for competitive reasons.

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

And just on the return on capital, Josh, as you look at the math, we put about 10% statutory capital in the business, and this is a 3% margin kind of activity, which creates a significant amount of incremental return on capital for us. And since all this is organic growth and not any kind of acquisition growth. I mean it's highly accretive to the overall cost of capital to the company.

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*

I have a few follow-ups. I guess, first on utilization, there's some thought that some of the March trend could be related to calendar dynamics around Easter versus more sustained change in the trend. I guess, could you maybe just give us your view here?

And then also be curious if you're seeing any changes in the level of acuity of patients that are showing up for care. And then Susan, could you maybe talk about what's driving the EPS seasonality this year? I think you've guided for over 80% of earnings in the first half of the year. Is it mainly the result of that expense timing that you mentioned in response to A.J.'s question? Or is there any other dynamic that we should consider?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes, Nathan, in terms of the first quarter and utilization seasonality, I would say, common, this is leap year. So all of things being equal, you would have had a higher trend in February because of leap year. But then there was other workday seasonality over the quarter such that we would say, in total, there's really not a seasonality impact and relatively consistent with the prior year. And those are all things we would have anticipated in our initial plan and then the guidance we gave for the first quarter. .

In terms of acuity, I would say aside from just again, the impact of the utilization management changes, where we always anticipated that effectively lower severity short-stay events would end up moving into the inpatient cost category versus the previous observation, which we reported ER. So that, we certainly are seeing, as I said, we need some additional time to see how the unit cost ultimately develops.

Some of the early indicators do suggest those are on average lower unit cost, which makes sense, but we need, again, because of the Change disruption, just some more time to fully evaluate that. But aside from that, I would say, again, limited visibility because of some of the disruption to the more recent periods in terms of claims submissions. But with what we do have, I'd say nothing that has caused us any concern from an acuity standpoint.

In terms of EPS seasonality, I would say the biggest driver of the differences you see every year and the disproportionate first half proportion is going to be just, in general, the lower proportionate contribution of the MA insurance business to the total than prior years. And so you're going to have PPD, which is disproportionately first half of the year, obviously impacting the first quarter, investment income and all those other things that are developing as they would in normal course, are just going to result in more earnings in the first half of the year just because MA proportionally is much lower, obviously, given the overall EPS and earnings expectation for the year.

Admin certainly has some seasonality to it, but I would say nothing unusual as we think about the year. The only thing that we did see because of the lower enrollment this year, you do see some positive impact in commissions. That is partly what we're seeing in the first quarter. And so that, based on the level of growth we would expect could develop a little bit differently. Again, those are things we will plan for. But aside from that, I see nothing in particular to call out in terms of admin seasonality relative to typical.

Operator

Our next question will come from the line of Andrew Mok with Barclays.

Andrew Mok

You revised your individual MA membership growth target up 50,000 versus your initial expectations of growth for 100,000. Hoping you could elaborate on the drivers of that. Was that just conservatism on your end? Or did you see any unexpected changes in the distribution channel during the open enrollment period that resulted in higher membership.

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

I would say the main difference is just how we performed in OEP. And I think that's a combination of a few things. I think it's some of our competitors having challenges in servicing their growth has been a benefit to us, and we've seen some recovery from that.

And the second thing is the actual performance that we've had in the nonduals area and the ability for us to continue to grow in markets that we have -- that are both competitive.

The third thing I would say is that what we've seen even in times that we are less competitive in the marketplace that our brand stands out and the stability of our brand, both from our service point of view and from our quality point of view, overcomes a lot of the benefit differences that we have in the marketplace. And I think in the OEP side, we saw that.

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. And just to add to what Bruce said, the increase was largely attributable to non-D-SNP sales, retention in total was largely in line. We saw in the OEP higher volume than we had expected, both in agents and switchers from other MA. And so as we think about the rest of the year, some of that agent favorability drove the increase. The switcher is obviously less so once the OEP ends.

And then as we've said, the progression from current to the year-end is also impacted by the redeterminations that will continue throughout the rest of the year. There's a little bit of less visibility into that because of the Change Healthcare issue where we rely on them for dual eligible status verification. So we'll continue to see how that develops. But that's why you can see the full OEP, not fully run rating through the end of your estimate.

Operator

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

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

Could you talk a little bit with the CEO transition as to Jim, what your impressions of the opportunities are? Are there any value creation opportunities that maybe are more structural or larger in scale, like outsourcing PBM or things like that? And have you guys made any sorts of operational changes in leadership or structure, again, contemplating both the market dynamics and the CEO transition?

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

Thanks for the question. This is Jim. No, there are not any changes to the team. So let me hit that one real quick. Second, are there opportunities? We're still in the process of evaluating opportunities. We certainly believe that there will be a continued need to drive efficiency. That's both on the operating side as well as continuing to get stronger in how we do medical cost management over time. We're still evaluating those opportunities. And the expectation is that by the end of the year, we would have more to say about where exactly the opportunities are and how we intend to go after them over time.

Operator

Our next question will come from the line of Lisa Gill with JPMorgan.

Lisa Christine Gill - *JPMorgan Chase & Co, Research Division - Analyst*

Susan, I want to go back to your comments around the PDP and the IRA for 2025. Can you talk about what you've seen for conversion over to MA in '24? And then how are you thinking about stand-alone PDP in 2025? Will that become unprofitable on a stand-alone basis? And then just secondly, I just want to understand, when you talk about the update for the bid strategy, will it be a separate press release? Or are we waiting for Q2 to get that update?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. So in terms of the IRA impacts and our thinking on stand-alone Part D, your first question around PDP conversions, I would say we continue to see a disproportionate opportunity to capture movement from Humana PDP members to Humana MA. For those members that choose to convert to MA, and we have visibility, right, in terms of any MA offering they choose. We tend to get a higher market share of those individuals that are making that decision than we do in just the overall individual MA space. So that continues to be very positive.

The absolute volume is somewhat lower just because of the overall lower membership growth that we're seeing this year, but that sort of advantage continues to hold as we've seen in the past. As we think about our stand-alone Part D strategy for '25, I would say we're very oriented to risk mitigation, just given the magnitude of the changes and the sensitivity that you will have in terms of the profitability of underlying membership based on sort of the level of utilization and specialty utilizers in particular. Given how our plans are positioned today and the limitation of only having 3 plans, which we have in market today, our goal will be to minimize sort of any risk inherent in our offerings and take probably a more cautious approach to see how the industry ultimately responds to the IRA changes, how the business, the health plan performs in light of those changes and then reassess frankly, for 2026.

As we suggested, it is -- we will see some larger premium increases for sure on some Part D plans, while others may have less so depending on their mix. And so that could drive some opportunity, as we said, for MA, and that's something we'll continue to evaluate. So that's how we're thinking about 2025, just given the level of changes and I'd say a lot for the industry to learn as we navigate through it. And I can't remember if there was one final question at the end that I didn't address. Did I cover everything?

Lisa Christine Gill - *JPMorgan Chase & Co, Research Division - Analyst*

Just, will it be a separate press release around your bid strategy? Or is that something that you'll update on Q2?

Susan Marie Diamond - *Humana Inc. - CFO*

Yes. I would imagine we will likely do that on the second quarter call. I don't know if we're scheduled at any conferences in between. My guess is, no. But my guess is it would be the second quarter call.

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

Well, thank you for your time and interest today. In closing, I would reiterate that Humana had a solid start to 2024. And while we acknowledge that the entire MA industry is navigating a difficult near-term environment, we continue to believe the strong fundamentals and growth outlook of MA and value-based care remain intact and the strength and scale of our platform and differentiated capabilities will allow us to effectively manage through the uncertainty, compete effectively and deliver compelling shareholder returns over the long term.

We appreciate your continued support and look forward to providing updates on our performance and outlook throughout the year. Have a great day.

Operator

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