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HUM.N - Q4 2025 Humana Inc Earnings Call

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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 fourth-quarter 2025 earnings conference call. (Operator Instructions)

Please be advised that today's conference is being recorded. I would now like to hand the conference over to your speaker today, Lisa Stoner, Vice President of Investor Relations. Please go ahead.

Lisa Stoner - Humana Inc - Vice President, Investor Relations

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; and Chief Financial Officer, Celeste Mellet.

Before we begin our discussion, I need to advise call participants of our cautionary statement. Certain of the matters discussed in this conference call are forward-looking and involve a number of risks and uncertainties. Actual results could differ materially. Investors are advised to read the detailed risk factors discussed in our latest Form 10-K, our other filings with the Securities and Exchange Commission, and our fourth-quarter 2025 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.

All 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, the call is being recorded for replay purposes. The replay will be available on the Investor Relations page of Humana's website, humana.com, later today. With that, I will turn the call over to Jim.

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

Thank you, Lisa. Good morning, everyone. Thank you for joining us. Let me hit the headlines. We are pleased with our solid 2025 performance. We continue to feel good about our membership growth. We remain committed to a consumer-centric strategy that is responsive to what our patients and members want to need. And we also recognize that to do that, we must deliver a stable and compelling margin. That requires regularly adapting to our funding environment. We will continue to do this to adapt to a funding environment to ensure that we stay on track with unlocking the earnings potential of the business by 2028 as we laid out at our 2025 Investor Day.

Now, I will briefly describe the progress we are making operationally. And as usual, I will frame my comments today around the four drivers of our business. That is, first, product and experience, which drive customer retention and growth; second, clinical excellence, which delivers clinical outcomes and medical margins; third, highly efficient operations; and fourth, our capital allocation and growth in both CenterWell and Medicaid. I will wrap up with additional commentary on the advanced rate notice. Most of my time today will be spent on Medicare product and experience and given the continued concerns that have been expressed by the market.

So let me start there. First, let me clarify what I believe are the real questions related to growth. Is this quality membership with attractive economics? Can we operationally absorb the growth and are we sufficiently positioned to fund the growth?

Second, let me take a moment to remind everyone how we think about growth. Our focus is on maximizing customer lifetime value and customer NPV. To maximize life to value and NPV, two things must be true: we must be priced appropriately to a sustainable and compelling margin and we must retain our membership year over year.

The way that we do that is by investing in an exceptional experience that fuels improved health outcomes and member retention. We also have moved away from past strategies built around loss leader plans. We design all of our plans to be priced to a sustainable margin adjusting for Stars.

Third, let me provide an overview of our growth and why we like the growth. We grew by approximately 1 million members or 20% in AEP. Our retention rate improved over 500 basis points year over year, and I keep emphasizing that that is good growth.

Over 70% of our new sales were switchers from competitor plans. On average, switchers had better economics. Now, I recognize that there are concerns about switchers from plan exits that our competitors have done. We did not have a high percentage of members impacted by competitor plan exits. We absorbed approximately 12% of these members. That is notably less than our market share.

70% of new sales were in contracts with 4 Stars or better and nearly 30% of our new sales were bounce-back members. So these are members that we have seen before in previous years. We recognize them, and we are pleased with the mix. Over 75% of our new sales were from higher lifetime value channels, so they're from better sales channels. This is nearly a 10 percentage point improvement year over year. And again, we view this as a very positive development.

When we look at full-year 2026, we do anticipate individual MA membership growth of approximately 25%. And I will continue to remind everybody that as we collect new information and as the market evolves, we are continuing to manage our go-to-market strategy dynamically. We have levers to pull if and when needed, and we are constantly evaluating that.

Now, fourth, let me briefly touch on the economics of our growth. We expect our new members to be accretive to the enterprise in 2026. We also continue to expect that when normalizing for Stars, our 2026 pricing results in a doubling of individual MA margin year over year.

My final point on growth is that we feel good about our operational capacity to absorb the growth. As we previously stated, this is a focus area for us. We are committed to not outgrow our operational capacity and to ensure a quality experience and quality care for our members.

We have been very much managing this proactively. The early signs on our ability to onboard are positive. In January, during the height of onboarding, I'll touch on just a few examples, we reduced our complaints to Medicare year over year. We improved our transactional Net Promoter Score, so this is a measure of customer service when members interact with our service center or contact center. And we increased our completion rate for health risk assessments. And I'd also just point out that complaint to Medicare CTMs and health risk assessments, HRAs, these are both Star metrics, where we are ahead of where we were a year ago in both of these areas.

So let me close with this: we expect our growth to be accretive in year, but more importantly, it further fuels our ability to unlock our earnings potential by 2028 as we laid out at Investor Day. In recognition of the high level of interest in our overall growth strategy, President of Enterprise Growth, David Dintenfass, will join Celeste, George, and me again today for Q&A.

So now, let me briefly turn to clinical excellence and touch on our Stars performance. Efforts to strengthen our Stars program continued to progress as anticipated. Our outlook remains the same as previously communicated.

We feel good about our operational progress so far. We continue to be confident that we are on the right track to return to top quartile Stars BY '28. Once the hybrid season is complete next quarter, we will provide some additional visibility into our final operating results. However, we will not speculate on thresholds.

Turning to highly efficient operations, we are making meaningful progress, which is evident in our 2026 admin expense ratio. Celeste will provide more color on the drivers of this improvement. And regarding capital allocation, we continue to grow our Medicaid and CenterWell footprint. Medicaid now spans 13 states, including Georgia and Texas, which are anticipated to launch next year.

We also hope to soon announce a strategic acquisition in the primary care space. Celeste will also provide color on our capital efficiency efforts that ensure that we have the capacity to fund both our member growth and some continued M&A while protecting our credit rating, which is a priority.

Before concluding today, I also want to touch on the advanced rate notice. I understand, I recognize that there is concern around the rate notice. As I have said in the past, Medicare Advantage sits at the intersection of US fiscal pressures and a program that is incredibly popular with seniors.

Every administration wrestles without these two forces. We are committed to always protecting our consumers the best we can, and we are very aware that we must do that within the constraints of the annual funding environment. If that funding environment cannot fully support our benefit structure, then we will adapt as we have in the past. But right now, we must wait and see where the final rate notice comes in.

So in conclusion, we expect to keep moving forward with margin progression in 2026 adjusted for Stars. We continue to feel good about the way our member growth is setting us up for this year in subsequent years. We are making progress on Stars. We will adapt to the rate notice once it's final.

Before turning it over to Celeste, I am pleased to share that Aaron Martin joined the company in January as President of Medicare Advantage and a member of the Enterprise leadership team. Aaron joined Humana with vast experience in healthcare, including a focus on making healthcare more convenient, engaging, and valuable to customers. He will be working closely with George and the team over the coming months and will elevate to the President of Insurance role upon George's retirement. We're excited to have Aaron on the team and expect that you have the opportunity to hear from him later this year.

With that, I will turn it over to Celeste for a few remarks before we go to Q&A.

Celeste Mellet - Humana Inc - Chief Financial Officer

Thank you, Jim. I will begin by echoing a few key messages. First, we delivered on our commitments in 2025. We reported adjusted EPS of \$17.14 in line with expectations and above our initial guidance of approximately \$16.25 while electing to make higher than initially planned investments to accelerate our transformation and position us well for the future.

Second, we remain confident in our customer-led strategy and 2026 membership outlook. We expect new members to be enterprise accretive in 2026 on average. More importantly, we expect the membership to drive significant lifetime value further fueling our ability to unlock the earnings potential of the business by 2028 as laid out at our Investor Day.

Third, we always take an appropriately conservative approach to final guidance. For 2026, the level of conservatism in our initial guide is higher than typical to account for the dynamic environment. Fourth, we are confident in our ability to fund the 2026 membership growth and are comfortable with our capital and our debt to cap levels.

Finally, we are committed to delivering a stable and compelling MA margin and unlocking the earnings potential of the business by 2028. Our MA benefit strategy must and will contemplate the funding environment each year. We must drive sustainable earnings and appropriate returns to be able to provide excellent health outcomes and service for our members and our patients.

Turning to brief comments on 2025, our results for the year were underpinned by solid performance across the Insurance and CenterWell segment. The full-year Insurance segment benefit ratio of 90.4% came in slightly better than our guidance. The full-year ratio includes a benefit set aside for a potential doc fix in 2025, which was then invested in areas such as network management and increased administrative costs to support things such as technology and other areas that position us well for the future.

I will now pivot to further details on 2026. We expect full-year adjusted EPS of at least \$9 with the anticipated year-over-year decline driven by the previously communicated bonus year 2026 Stars headwind net of mitigation. We remain confident in the overall assumptions used in our 2026 pricing.

As a result, we continue to anticipate doubling individual MA pretax margin in 2026, normalizing for Stars. Meaning, if 95% of our members were in 4-plus Star plans consistent with 2025, we would hit doubling of individual MA margin in 2026. The expected underlying margin expansion is aided by clinical excellence and operating efficiency efforts, which are progressing as anticipated.

Further, early indicators such as risk scores, pharmacy claims, and hospital admits per 1,000 or APTs are in line with expectations. All in, after accounting for the '26 Stars headwind, our initial guidance assumes individual MA margins are slightly below breakeven.

Let me touch briefly on the Stars headwind. The net Stars headwind for 2026, including individual and group MA, is approximately \$3.5 billion. This is net of both contract diversification and provider offsets, which as a reminder, are lower than typical due to our Star support for providers.

When calculating the headwind for '26, it is important to keep the membership and revenue growth in mind, which is why the number is larger than what we have previously discussed with you. While we now have 45% of members in 4-plus Star plans for '26, our expected membership base will also be 25% higher due to the '26 member growth, which includes strong retention. Higher retention means that we kept more members on the 3.5 Star contracts than we previously expected. In addition, approximately 30% of new sales were on contracts rated below 4 Star to BY '26.

Turning to our ongoing efficiency efforts, we expect significant improvement in our consolidated operating cost ratio for 2026. The decrease is primarily driven by operating leverage from membership and revenue growth along with tactical cost-cutting and transformation efforts, partially offset by the impact of the Star rating headwind.

As outlined at last year's Investor Day, we have made meaningful progress on tactical efficiency improvements, including consolidating our supplier base and the early retirement program we discussed with you last year. These actions have contributed year-over-year operating expense ratio improvement.

Looking ahead, we expect our broader transformation efforts to increasingly impact results beginning this year. This includes expanding outsourcing capabilities, simplifying and standardizing processes, and leveraging technology and automation.

For example, our work with partners to outsource components of some corporate functions is progressing as planned and delivering improved capabilities and cost efficiencies. These items are just a sample of our multiyear transformation that is driving efficiency and changing how we operate.

I will now stick to the balance sheet and our plans for funding the '26 membership growth. As I discussed throughout 2025, we have been focused on efforts to increase the efficiency of our balance sheet and fortify our foundation. These initiatives include optimizing legal entity structures, refining, reinsurance and risk transfer arrangements, selling non-core assets, and managing the timing and structure of capital deployment.

Of note, the capital optimization progress made to date significantly reduces the required funding for expected membership growth in 2026. Despite expected premium growth of 40% from '24 to '26, our statutory capital requirements will increase by less than 20%. These improvements in capital efficiency will offset over \$3 billion of growth in our capital requirements from the end of '24 through '26, representing the overwhelming majority of the capital needed to fund 2026 membership growth while maintaining capital with a prudent buffer above regulatory requirements and rating agency expectations.

Finally, after contemplating capital required to fund '26 membership growth and select small to mid-sized strategic M&A opportunities, which we expect to fund with the sale of non-core assets, we remain comfortable with our debt to cap levels, which are expected to remain largely flat year over year. We remain committed to prudent debt to capital management and are focused on maintaining our credit ratings.

In summary, we are pleased with our solid performance in 2025 and believe '26 represents an important step forward on our journey of unlocking the earnings potential of the business by '28, including delivering a stable and compelling MA margin. I will turn the call back to Lisa to start the Q&A.

Lisa Stoner - Humana Inc - Vice President, Investor Relations

Great. Thank you, Celeste. (Event Instructions)

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Stephen Baxter, Wells Fargo.

Stephen Baxter - Wells Fargo Securities LLC - Analyst

We hear you on the membership growth being enterprise accretive. I mean, I guess, potentially, could you expand a little bit on the level of earnings that you can drive purely outside of the MA underwriting?

And then as we look at the MA underwriting margins in isolation, being slightly below breakeven. How would we contrast that against your retained growth versus the new growth that you expect to take on here?

Celeste Mellet - Humana Inc - Chief Financial Officer

Thank you for your question. So when we talk about enterprise accretive, we are including the earnings associated with CenterWell. So if you recall, last year, we had a headwind in CenterWell Pharmacy because of the decline in membership. This year, we have a significant tailwind in CenterWell Pharmacy associated with the new membership.

We also will have greater patients and at CenterWell PCO and expect to see an increase in home health volumes also related to the membership growth. And all of that growth across CenterWell is very positive from a margin perspective.

As it relates to individual MA margins, as I mentioned, we expect them to be just below breakeven in total in '26. While we don't provide cohort level margin information for competitive reasons, I'm going to give you a little more detail this year given the unique dynamics. So when you take the Stars headwind into account, the margins look largely similar for new and continuing members due to the following:

First, on continuing members, they're disproportionately impacted by the Stars headwind with the majority on contracts with less than 4 Stars. Absent the Stars headwind, as we've talked about extensively, the margin would be significantly better. New members are less impacted by the Stars headwind. So 70% are on 4-plus Star plans, but 30% are on plans with less than 4 Stars. They have a similar margin to the existing cohort for a couple of reasons.

One, the cost of acquisition, which is a little bit lower this year due to the actions we've taken, but still significant; and two, a higher MLR associated with the new members driven by: one, lower MRA if conditions have not been previously captured and, in some cases, potentially higher med costs if they have not been managed before joining Humana, so net-net, the overall margin for the existing and the new cohorts are fairly consistent but for very different reasons.

Operator

Justin Lake, Wolfe Research.

Justin Lake - Wolfe Research LLC - Analyst

I wanted to focus on kind of the trajectory forward. To Steve's question, you're losing -- you have slightly below breakeven margins in the Insurance business in the new members. Can you talk a little bit about how I'm estimating you got about 2.5 million new members here to Humana. It's a huge cohort. How is the typical progress we think about removing Stars in the equation. What's the typical progress in margins over a three- to five-year period? How should we think about that cohort becoming accretive?

And then Jim, your comments on getting back to 75%, or should I say, the top quartile on Stars. What would be the net benefit in 2027 from that approximately compared to the \$3.5 billion headwind you had this year on a net basis.

Celeste Mellet - Humana Inc - Chief Financial Officer

Justin, I'll take the first part of your question. George may add to it, and then Jim will. So in terms of the margin progression. If you think about like from year one to year two, you have a pretty substantial pickup as you have a more normalized marketing load. So your marketing load takes around five years to fully run out.

But it typically will be cut in half between the first and the second year, the first and second year, though slightly less because of some of the actions we took this year, some of the levers that we pulled.

Second, you have an improvement in your medical benefit ratio throughout the period. So you'll have an improvement in the second year than the third year than the fourth and even in the fifth is probably where it normalizes. So you should have a fairly substantial increase in the first year with the combination of the marketing load being lower and then that improvement in the MLR and then slow improvement on the cohort in the years after that. George, anything you might add to that?

George Renaudin - Humana Inc - President - Insurance

Yes, Celeste. Thanks. The other things that I'd just think about as you onboard members move them through their experience with us, just three other things to think about that helps improve the margin as well. First, of course, is MRA, which as we continue to work, coding, getting members appropriately coding the follow-up care that they need as a result of the assessments that we do. We find an improvement in both the coding and in their medical management.

And that the second part of that micromanagement also is able to kick in. We have many programs, many value-based programs as well as our care management programs that will take effect and that helps in the ongoing years. And third, if you think about how the membership comes in, they come in and typically there's a lower share of them that are paneled to value-based partners, our well-performing value-based partners.

So as they progress through they become more and more paneled to those well-performing value-based partners, which also helps improve the margin over time. So there really are 3 major impacts that happen as those numbers come in and as we get them into our programs and provide better outcomes for them.

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

Yes. Let me jump into the Stars question. I presume the nature of the question is you're trying to understand the difference between 95% of membership in a 4-star plan and our metric of 75th percentile, that -- what is that delta.

The -- let me remind everybody that we have chosen to anchor on 75th percentile for two reasons. One is, as changes in policy change the nature of Stars performance across the entire industry, it is better for us to index to the industry than to a specific number.

Obviously, anything that changes across the industry, you would expect to be incorporated into pricing benefits over time. And so it wouldn't have a net impact on margin or overall profitability, but it could have an impact on the revenue.

And the second reason that we anchored on 75th percentile is that from a planning perspective, we felt it was prudent to anchor on a place that gave us some planning flexibility over time. And so that was the rationale for 75th percentile.

The challenge that we have in giving you a specific number is that this does at the end of the day, tied back to where is the industry performing and what are the policy changes impacting Stars. So we don't have a specific number that we can give you around that. But what I would again emphasize and I know I just said this, but whatever that number is, if we're at the 75th percentile, we feel comfortable that we can accommodate that in our pricing and our benefits in a way that will not have an impact that we should be able to achieve our margin expectations over time.

Celeste Mellet - Humana Inc - Chief Financial Officer

And if I can just add, Justin, in the numbers we laid out for you at the Investor Day, we -- that 2028 number reflects -- or the math, as I told you guys to do reflects Stars at the 75th percentile. So that is the headwind of not being at the 95% is reflected in what we've laid out for you.

Operator

Ann Hynes, Mizuho Securities.

Ann Hynes - Mizuho Securities Asia Ltd - Analyst

How did your expectations for 2026 change versus your thoughts on Investor Day? I know you didn't give guidance, but you did say 2026 would take a step back. I think the step back is probably a little steeper than what we thought. Can you just provide what the big deltas were from then to now?

Also, you said in your prepared remarks that the guidance is more conservative this year than normal years. Can you just go through what product guidance do you think is the most conservative, that would be great.

Celeste Mellet - Humana Inc - Chief Financial Officer

Ann, I think the biggest difference between where we were at Investor Day and where our guidance played out is really the embedded conservatism in our numbers. So within the assumption themselves, we tend to always have conservatism in MA, given that we don't have a full picture until later in the year. Based on what we have today, we feel very good about where we are.

In terms of our trends, I'll share with you what's embedded in the guidance, but what we did in the end is basically haircut where we landed just given our known headwinds and tailwinds. So while some of the assumptions have conservatism embedded, there's just a broader haircut. So what's embedded from a trend perspective is cost trends that look a lot like 2025, but slightly higher for a reason a layout.

So as a reminder, we assume the higher end of mid-single-digit medical costs for 2025 and low double-digit Rx trends. That is about where we landed. So '26 would be similar, though higher because of the lack of doc fix in 2025 and the inclusion of doc fix in 2026.

Operator

Ben Hendrix, RBC Capital Markets.

Ben Hendrix - RBC Capital Markets Inc - Assistant Vice President

I wanted to zero in quickly on the 140,000 new D-SNP members, 18% growth there. Just if you could kind of frame how that compared to your expectations both in the absolute number and then also on the profile, where they bounce back members? Did they come from exited communities from your competitors? And the degree to which they're handled to your value-based partners?

George Renaudin - Humana Inc - President - Insurance

Ben, thanks. This is George. So on the D-SNP, the absolute number is higher than expectations because our overall growth is higher than our initial expectations. But as a percentage, it's slightly lower.

So that's the way to think about the D-SNP membership. Now to your other questions, as Jim said in his opening remarks, we did not gain our market share, if you will, of those planned exits from our competitors, and so that holds true across the business.

And to your last question about value-based partners, as I said, the membership comes in oftentimes not paneled at the same level as our ongoing block of business. And we would effect as we do every year that the amount of paneling to increase year-over-year.

Now having said that, our duals because most of them are on HMO products do tend to come in panel. So when you think about the dual membership versus our core membership, the dual membership would be a greater share panel compared to the overall block of business.

Operator

Joshua Raskin, Nephron Research.

Joshua Raskin - Nephron Research LLC - Analyst

I apologize sort of redundancy and where I think I'm going. But as you mentioned, the individual margins that are slightly negative in 2026. So going back to the Investor Day from June, is there anything you've seen that changes your view of the ultimate margin profile of this now larger book of business?

And as you look out to 2028, and specifically interested in any updated views around obtaining that top quartile Stars rating as well as perhaps the impact of the 2027 rate notice?

Celeste Mellet - Humana Inc - Chief Financial Officer

Josh, I'm going to take a crack at your question and then Jim will jump in. So as you think about 2028, I want to remind you of our scale. So with the growth this year, it gives us quite a jump on achieving the 2028 target.

So if you look at the operating cost ratio, the improvement is fairly significant, even accounting for the Stars headwind, and that's really driven by the operating leverage from membership and revenue. The cost cutting that we've talked about is consistent with what we talked -- spoke with you about at the Investor Day, we're on track for that.

And then the operating leverage does reflect the investments we made in onboarding and ensuring that we have the right capabilities in place with the expanded medical base -- with the expanded member base. So we are ensuring we spend the money to do it right, but still have the significant pickup. So I think about the step forward in terms of operating leverage.

And as I mentioned in my opening remarks and Jim mentioned as well, we are going to -- we'll adapt to the funding environment. So we expect to continue to make good progress on 2028 and feel good about our trajectory so far.

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

Yes. So let me hit Stars, and I'll touch on the rate notice as well. On Stars. Again, what I'm going to emphasize just philosophically is the single biggest thing that we were adjusting to as we went through AEP and as we considered OEP and , is our ability to onboard a big portion of that is what can we absorb from a Stars standpoint.

Again, there's always so much that you have clear visibility into early in the year. We tried to give a couple of examples there with both CTMs and with the RAs, where we do have some early look at progress and progress is actually quite positive. And to be clear, that's not on an absolute basis. That's on a per member basis. That is adjusted for the cohort who is onboarding.

The other thing I would point out on Stars, there's a couple of things that we are doing differently versus two years ago that also better positions us to manage a large new member cohort. One is we are simply starting our programs earlier in the year. So if you went back two years ago, we would really start most of our proactive programs in the second half of the year and sometimes as late as the fourth quarter of the year.

Most of those are starting late first quarter, early second quarter when we get our initial data on those members' health status. The second thing that I would point out is we have gotten much better at using that data to do appropriate targeting to understand who very early in the year has already cleared a whole bunch of Stars metrics. And therefore, where do we devote our resources to close gaps for those who have open gaps. So both of those things just put us operationally at a much better place to handle Stars.

Now look, I'm also just going to state the obvious. This is Stars. It is a relative score. There is always risk in this. Can we say that there's no risk?

Of course, we cannot, but can we say that we feel good about our ability to mitigate that risk? Yes, this has been very much top of mind. So let me flip to rate notice here for a second. I don't know that I have a lot to add over my initial comments. I think everybody is well aware that the advanced rate notice is -- came in below medical cost trend, like that's not new at this point.

We recognize the pressures that are constantly being balanced here. We are doing what we can to advocate for our members and our patients to make sure that we get to an appropriate funding level that protects their interests. And at the end of the day, this is a difficult dynamic, but we will adjust to wherever the final rate notice lands. Like that is the bottom line. Wherever we end up, at the end of the day, we will adjust to that. And between now and then, we're going to do everything we can to advocate for our members.

Operator

Scott Fidel, Goldman Sachs.

Scott Fidel - Goldman Sachs Group Inc - Analyst

Can you give us some detail into -- relative to the 25% overall MA growth, how that breaks down in terms of PPO versus HMO in terms of the relative growth rates that you're seeing across there? And then also in terms of relative to the metric had around the percentage of new members that you gained from competitor exits, maybe holding on the PPO specifically, what percentage you estimate for the PPO product?

David Dintenfass - Humana Inc - President - Enterprise Growth

Scott, this is David. We won't be able to disclose all those details. But what I would say is this is that between HMO, PPO and frankly, across our plants, we've tried to have a reasonable margin across all of them. That's part of the new strategy is not to have higher margin and lower

margin plans, going to be worried about outgrowth and the lower margin plans. So we can't disclose the exact growth rates, but the ability for both of those to be accretive much more balanced than it has been in the past.

Operator

AJ Rice, UBS.

AJ Rice - UBS AG - Analyst

I appreciate all the comments about different aspects of operating leverage and so forth. But just to make sure I got the right perspective on it. I think at the Investor Day, you talked about the transformation initiative broadly, having an improvement from '25 to 2028 of \$1.6 billion to \$2 billion in pretax earnings.

I know there's a lot of things going on this year, but in your '26 outlook, how much of that will you have realized this year, if any? And how much sort of progressively do you expect to get over the next few years to get to that level. I don't know if there's upfront cost. So maybe it's not having any impact to positive this year, but just some flavor for how we can sort of track how you're progressing given that's a big part of the -- getting to the earnings power of the company for '28?

Celeste Mellet - Humana Inc - Chief Financial Officer

Yes. Thanks, AJ. So there -- as I said before, there are two components of the operating leverage. There's the revenue growth, which is driven by member growth and then growth in CenterWell and then cost savings. So in terms of member growth and the pickup at least from a member volume perspective and CenterWell, we have -- we are close to where we would have expected to be in 2028.

In terms of the cost cutting, we are only just beginning, so we expect a significant pickup in '27 and then 28. So we still have quite a bit to go the same sort of trajectory as we talked about at the Investor Day. We've been very deliberate about how we do the cost cutting. We want to ensure that we do it in a way that makes sense and is sustainable and doesn't put the business risk -- business at risk as we do it.

So still quite a bit to go there. So we continue -- we expect to continue to see upside there. Let me also remind you that we expect continued growth in terms of our clinics in CenterWell as well as progress in some of the strategic initiatives on the pharmacy side that we've talked to you about.

And we also expect to continue to see improvement in the margin in group MA. We did have, before the Stars headwind this year, a 500 basis point pickup due to recontracting efforts. There's still several hundred basis points to go. We still have upside in Medicaid as we continue to move through the J-curve and then moving through the J-curve also on the CenterWell PCO clinics. So all in, we still think there is upside through both the overall work we're doing on margin improvement as well as the cost cutting.

Operator

Jason Cassorla, Guggenheim Partners.

Jason Cassorla - Guggenheim Securities LLC - Equity Analyst

Great. Maybe just looking back to 2025, your investment spend that you spiked out appears to be peers have totaled well over \$550 million, which seemingly indicates that your individual MA business outperformed pretty well this year, kind of netting against those investments.

Can you remind us how much of that investment spend is run rating into 2026? And I guess, relative to how you're thinking about guidance and our conservative posturing, are you taking a similar approach in terms of spending away any outperformance this year, or can you frame how you're thinking about further investment spend?

Celeste Mellet - Humana Inc - Chief Financial Officer

Yes. So let me hit the first part. So we -- your estimate is close to about right in terms of the incremental investments. We did -- we do have a lot that we want to do to transform the company, and we did invest there. As it relates to this year, we are not currently contemplating any incremental investments.

We are continuing to just generally invest in the company. We are not cutting back on tech investments. In fact, that's a little bit higher. So we're not starving the business as we move forward. We're trying to balance the short term and the long term, but we are being very mindful of our spending.

And then in terms -- and as it relates to Stars, we talked about last year being a transition year. So the overall Stars investments on a PMPM basis are down that's driven by sort of scaling back in some of our old programs and scaling up some of -- a lot of the new programs, including the work we're doing about member onboarding and some of the other things that Jim spoke to you about.

We've also found much more efficient ways to improve Stars. So overall, actually, our Star spend is fairly consistent with last year on an absolute dollar basis, but on a PMPM basis, it's down significantly, and that's driven by the 25% membership growth. And I forgot the second part of the question.

Jason Cassorla - Guggenheim Securities LLC - Equity Analyst

Just if you were going to some incremental investments for --

Celeste Mellet - Humana Inc - Chief Financial Officer

Sorry. We -- if we decide to do that, which we may, we will be very transparent with you if we decide to make incremental investments throughout the year. We will share that with you, so you understand the operating performance versus where we might be offsetting it with investments.

Operator

Ryan Langston, TD Securities.

Ryan Langston - Cowen and Company LLC - Analyst

On the higher level of bounce back membership recapture, is there a way to generally think about how long those members have been away from Humana. And then v28, I think you previously said it's about a 160 basis point impact just given the sort of level of new growth. Is that still in the ballpark? Or is there anything to add there?

David Dintenfass - Humana Inc - President - Enterprise Growth

On the bounce back, we'll be able to disclose specific details. We look back over several years to say where have the members in bouncing back. And obviously, the more recent membership is a bigger percentage of the overall, but we look back several years to say which members we actually have previously experienced with, and that's the close to 30% number. I missed the second part of the question --

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

Yeah, v28, yes, your number is correct. Nothing has changed there. Yes.

Operator

Elizabeth Anderson, Evercore ISI.

Elizabeth Anderson - Evercore Inc - Analyst

I was wondering if you could talk in a little bit more detail about the change in EPS seasonality this year. It's a little bit different than prior skews. So I just wanted to better understand if that's all IRA related or if there's anything else involved in there? And then any early comments that you guys can share on OEP in terms of what you're seeing in terms of additional retention or anything else there?

Celeste Mellet - Humana Inc - Chief Financial Officer

Yes. So the seasonality is a bit different than last year. The underlying factors are the same. So the IRA is driving steeper curve, a steep curve, but it's, I guess, aggravated, if you will, by the Stars headwind. So as you have the loss of operating leverage from Stars, and that sort of aggravates the second half of the year versus 2025. But otherwise, outside of Stars, the trajectory would be very similar.

David Dintenfass - Humana Inc - President - Enterprise Growth

And Elizabeth, you asked about AEP. It's a little early to know. Again, we quoted a 500 basis point improvement in AEP. I think for OEP, it's too early to know, but we do think there's upside to that. I mean we like the momentum. As Jim said, we're liking the transactional NPS. There's a lot of indications that our member liking the benefit stability. And so we do think there's upside, but it's just early to have a number.

Operator

Kevin Fischbeck, Bank of America.

Kevin Fischbeck - Bofa Merrill Lynch Asset Holdings Inc - Analyst

Great. I wanted to ask about 2027 thoughts. Obviously, you're not concerned about how things are going to play out from a cost perspective in '26, but the market is. I want to understand how you guys believe your visibility is going to play out over the next several months? Is there anything you're doing extra to make sure that if there is an issue, it is in fact captured before you have to submit bids for 2027?

And then it's not clear to me what you mean when you say you're going to factor in the rate environment for 2027. We've seen a bunch of companies more recently just say we're focusing on margin wherever membership lands, it lands. And the market seems to like that. But your LTV commentary seems to leave some wiggle room to kind of say, no, I need to retain members. So like what does it mean like to adjust to the rate, are you going to immediately go back to the margin trajectory you were on, or are you going to have to balance margin and membership growth when you think about LTV?

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

Yes. Thanks for the question. On the first half of that, we have a good look at member performance by around April, and then we have a better look in May. And both of those views are early enough that if we need to make adjustments in the bid, we can make adjustments in the bid. So we should have a solid enough understanding of what the current cohort looks like at the time of bid and be able to incorporate that in, so we feel good about that. And by the way, that is no different than other years. So we feel good there.

On the second half of the question, yes, look, let me be clear. We made a set of commitments to ourselves and to investors at Investor Day last year, and we are standing by those commitments. And so our focus is on retaining membership to be sure, but it is on getting the first goal is to get to the margin trajectory that this business needs to be on over the long term, right?

Like we are focused on getting to the right long-term, sustainable, durable, attractive margin. And -- and yes, we're going to retain as many members as we can along the way. Are we focused on new member growth? No. Like new member growth is not the focus. It is great experience, it is retention and it's getting to the right margin profile.

Operator

Erin Wright, Morgan Stanley.

Erin Wright - Morgan Stanley - Analyst

A two-part question here and going back to the rate notice, but is there anything specifically on the rate notice that you would have outsized exposure to relative to the industry from a coding perspective? Or can you talk about some of those components of the rate notice and how you're thinking about that?

And then just from a statutory capital perspective, the requirements there, the more favorable positioning. Was that associated with the emphasis of certain states or jurisdictions? And is there more to do on that plan and -- or more to accomplish there? And then just your capital deployment thereon.

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

We're now focused on the second question. Remind me what the first question is?

Celeste Mellet - Humana Inc - Chief Financial Officer

The rate notice.

James Rehtin - Humana Inc - President, Chief Executive Officer, Director

The rate notice, yes. So on the rate notice, the -- first of all, we're still working through some of the detailed analysis. But the high-level message is that changes that have occurred from a policy standpoint this year do not have the same type of variance that v28 had. In general, most of the industry should be impacted around a pretty narrow band around the and so even as we're working through some of the details, we feel pretty confident everybody is going to be a margin of error around the industry mean.

Celeste Mellet - *Humana Inc - Chief Financial Officer*

Yes. In terms of the capital efficiency activities, we have done most of the work that we think makes sense in terms of redomestication which is really focusing on moving around the legal entities. There is more work that we can do that there is more opportunity for us on some of the other areas, including reinsurance.

So we'll -- we still have those in our pocket as we think about going into 2027, et cetera. But overall, we're very happy with the progress we made and expect to continue to really focus on ensuring that we have the right amount of capital in place but not too much, which becomes a drag in terms of our overall efficiency and our ability to invest in other areas.

Operator

Matthew Gillmor, KeyBanc.

Matthew Gillmor - *KeyBanc Capital Markets Inc - Equity Analyst*

I wanted to ask about value-based contracting. Can you just remind us the proportion of MA members that are capitated versus the risk models. And is there any comment in terms of how that's changed as you think about 2026 in future periods?

George Renaudin - *Humana Inc - President - Insurance*

Thank you for the question. I appreciate that, Matthew. So the percent of membership is relatively the same, about a third in risk, a third in value-based, other types of value-based, and then the third that are in either nonvalue based or just some basic pay for performance. One of the things that I mentioned before is that when you have an influx of members, generally, that number comes down a little bit at the start of the year and as the year progresses when members are choosing primary care doctors and/or we have claims-based attribution of members into panels.

That number builds back up. So that's the typical thing we see. We work with many highly performing value-based partners and do not have really a significant percent of our membership with any particular provider. And we continue to see value-based partners, wanting to grow with us. We have many value-based partners that we've been speaking to as recently as in the last month or so that want to expand significantly with us.

So we feel good about where we are with the value-based partners. And very much appreciate all the good things they do for our members to contribute to better health outcomes and higher quality care.

Operator

Lance Wilkes, Bernstein.

Lance Wilkes - *Sanford C Bernstein & Co LLC - Analyst*

Yes. I wanted to follow up on the value base a little bit. Just to ask, for '26, what's the impact to MLR, if any, of any changes to value-based care financial terms or carve-outs of thing, or is that fairly stable? And related to value-based care, what's the -- your sense of the capacity to absorb the magnitude of risk that you're talking about? And then just a quick cleanup question, in the incremental investments that you made in '25, what portion of that, if any, was in -- would have been in the medical costs or attributed to medical costs?

George Renaudin - Humana Inc - President - Insurance

Nothing really has changed with regard to the financial performance of the value-based providers as far as proportionately how they contribute to our margins. So what we've shared before in Investor Days and what we shared before, still holds true. I won't go into many details there because obviously, those contracts between us and our value-based providers are proprietary, but we do a lot of work with them to help support them to help them be successful in caring for our members and improving the health of those members, so nothing really has changed there from a value-based standpoint, except for I will say a couple of things we've talked about before.

The first is that we did provide significant support to them in 2025 by taking back the Part D risk, which given the volatility that, that can have at a relatively smaller number of membership for our value-based partners. We didn't think it actuarially made sense for them to take on that risk. So we took that back now significant assistance to them in '25, and we continue that into '26. That's why as we've said before, we also have done a lot of work to help mitigate the Stars impacts of '26. So we continue to work with our partners in a very collaborative way and appreciate the work they do for us.

Celeste Mellet - Humana Inc - Chief Financial Officer

And as it relates to the incremental investments, I'd say, 90% were in medical costs.

Operator

Whit Mayo, Leerink Partners.

Whit Mayo - Leerink Partners LLC - Analyst

Jim, any meaningful changes to your provider contracting strategy this year? I feel like I've heard provider contracting a couple of times on the call. So just wondering if something's changed to minimize that friction. And I guess I mean this through the lens of the Stars question around member satisfaction.

George Renaudin - Humana Inc - President - Insurance

Yes. There have been a number of things we've done. I just mentioned two with what we did with Part D and what we've done with supporting and mitigating the Stars headwinds. But we also continue to do many things across the provider landscape. We have a whole team that is looking at how we improve our contractual relationships with our providers in a number of ways, including, as you mentioned, reducing the friction.

We did make a large announcement last year about how we're improving the prioritization process to decrease the number of things that take prior authorization and to increase the automation of how we do prior authorizations as well. One of the things that we have continued to do and that we have historically been very good at, for example, is for both our rural and nonrural providers. We essentially pay on average those claims in under 15 days.

So we think that we also appropriately help our providers with their payment rates. So there are a number of things that we do to move and we have teams that are very much focused on improving those provider relationships and reducing the abrasion. They are oftentimes the face of Humana to our members, and we want to make sure that we maintain great relationships with them.

With that, I'm going to turn to the close. And as we close out, I'm going to start -- I'm going to end where we started with the key messages that we want to make sure everybody understands. Again, we're pleased with our 2025 performance. We continue to feel good about the membership growth. We remain committed to a consumer-centric strategy that is responsive to what our patients and members want to need.

And we recognize that to do that, we must deliver a stable and compelling margin. So I'm just going to say that again. We must deliver a stable and compelling margin. And that requires that adapt to our funding environment. We will continue to do that to ensure that we stay on track with unlocking the earnings potential of the business by 2028 as we laid out at our 2025 Investor Day.

With that, I would thank you for joining us this morning and for interest in Humana, and I want to say thanks to our 65,000 associates who serve our members and our patients every day. We appreciate your support and we hope you have a great day.

Operator

This concludes today's conference. Thank you for your participation. You may now disconnect.

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