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OVERVIEW:

Company Summary

REFINITIV

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Elevance Health Third Quarter Earnings Conference Call. (Operator Instructions) As a reminder, today's conference is being recorded.

I would now like to turn the conference over to the company's management. Please go ahead.

Stephen Vartan Tanal - *Elevance Health, Inc. - VP of IR*

Good morning, and welcome to Elevance Health's Third Quarter 2023 Earnings Call. This is Steve Tanal, Vice President of Investor Relations. And with us this morning on the earnings call are Gail Boudreaux, President and CEO; John Gallina, our CFO; Peter Haytaian, President of Carelon; Morgan Kendrick, President of our Commercial and Specialty Health Benefits business; and Felicia Norwood, President of our Government Health Benefits business. Gail will begin the call with a brief discussion of the quarter and recent progress against our strategic initiatives. John will then discuss our financial results and outlook in greater detail. After our prepared remarks, the team will be available for Q&A.

During the call, we will reference certain non-GAAP measures. Reconciliations of these non-GAAP measures to the most directly comparable GAAP measures are available on our website, elevancehealth.com. We will also be making some forward-looking statements on this call. Listeners are cautioned that these statements are subject to certain risks and uncertainties, many of which are difficult to predict and generally beyond the control of Elevance Health. These risks and uncertainties can cause actual results to differ materially from our current expectations. We advise listeners to carefully review the risk factors discussed in today's press release and in our quarterly filings with the SEC.

I will now turn the call over to Gail.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Thanks, Steve, and good morning, everyone. Today, we're pleased to share that Elevance Health delivered another solid quarter of financial and operational performance, reflecting the strength and resilience of our diversified portfolio of businesses.

Third quarter GAAP earnings per share was $5.45, including a charge we took during the quarter that I will discuss in detail in a moment. Adjusted earnings per share was $8.99, reflecting growth of approximately 20% over the third quarter of 2022. Our results demonstrate our ability to execute on our enterprise strategy of delivering whole health solutions that are affordable, personalized and simple.

Based on our strong year-to-date results and confidence in our outlook, we are increasing our guidance for adjusted earnings per share to be greater than $33 for 2023, which includes incremental investments planned for the fourth quarter that will accelerate our strategy and enhance the performance of our Medicare Advantage business. It is the strength and resilience of our diverse businesses that provides comfort in our outlook, while the earnings power of our health benefits and Carelon division provides us the confidence to reiterate our commitment to our long-term target compound annual growth rate in adjusted earnings per share of 12% to 15%.

Let me now turn to some highlights from our business segments. Starting with our Health Benefits division, which delivered robust third quarter results as we continue optimizing our diverse set of businesses while responding to a dynamic and evolving business environment.

In our commercial risk business, we are successfully executing on our goal to deliver operating margins in line with pre-pandemic norms. Retention has been consistent with our expectations, and we're pleased with our progress, which we expect will extend well into 2024.

In the employer market, we're delivering differentiated value where it matters for employers, affordability, experience and simplicity. Over the past 3 years, we've become the sole source medical benefits provider for 32 of our national clients, including 9 additional customers who will be consolidating their coverage with us effective January 2024. For large employers, we continue to deliver differentiated value and are seeing employers move away from point solutions and sliced offerings to selecting Elevance Health as their strategic partner for the integration of all of their medical benefits.

Consistent with these results, our advocacy solutions business, which provides personalized guidance and support to help members both navigate the complex health care system and optimize their health and well-being, will add 37 new clients in 2024 covering more than 550,000 members. This includes 2 large employers who are returning to Elevance Health after previously testing third-party advocacy vendors.

In the individual market, we are seeing strong growth in plans that offer affordable and comprehensive coverage designed around the needs of consumers in our communities, including those transitioning from Medicaid to individual ACA coverage. Year-to-date, our individual membership has grown by 27%. Through the first half of this year, the latest period for which industry data is available, our individual ACA membership growth rate more than tripled that of our competitors in our 14 Blue states.

Our government business also posted a strong quarter. In our Medicaid business, rates are actuarially appropriate, but we are absorbing a membership headwind related to the pace of Medicaid redeterminations, especially in states that have adopted accelerated time lines. Nearly 3/4 of all Medicaid beneficiaries terminated in our markets to date have less coverage for administrative reasons and 37% of the attrition from our own health plans has been driven by individuals under 18 years of age, many of whom may still be eligible for Medicaid benefits. We are doing all we can to ensure continuity of coverage for as many consumers as possible, working closely with our state partners to ensure individuals eligible for Medicaid retain coverage while also offering affordable ACA exchange plans in nearly all of our blue counties.

We are seeing encouraging signs. In some of our Blue states where we offer Medicaid and commercial coverage, we have seen 30% or more of our Medicaid members who were terminated prior to the end of June return or retain coverage with Elevance Health, albeit with gaps in coverage that can extend for several months. We expect re-enrollment to accelerate in the coming quarters as we continue with our omnichannel approach to

outreach and engagement, ensuring our members are aware of their options. Accordingly, we anticipate the rate of membership attrition associated with redeterminations will slow considerably in the coming quarters.

In Medicare, we continue to offer high-quality plans that provide seniors access to comprehensive and coordinated care, and we are committed to doing so for the long term. We're disappointed, however, with our Star's performance for measurement year 2022, which is the basis for star ratings that will impact the 2025 payment year and specifically, with our decline in consumer survey scores and the way in which CMS applied a new statistical methodology that resulted in significant increases to many Star measure cut points.

To improve our performance in future periods, we have already commenced investments in 4 primary areas: service, product, network access and operations. For example, in July of this year, we built on the success of our innovative advocacy model in the employer market by adapting it for the unique needs of Medicare eligible consumers. This new program, My Health Advocate, is a comprehensive, personalized and relationship-based customer service model that enables our members to effectively navigate the health care system, their benefits and ultimately, to improve their overall health and well-being.

Furthermore, we have enhanced our core and supplemental benefits to reduce members out-of-pocket costs for prescription medications simplified our dental benefits and strengthened our grocery and over-the-counter benefits. We're also simplifying consumer and provider experiences through the automation and elimination of certain prior authorizations, accelerating our work with value-based care provider partners and improving clinical decision appeal rates. Collectively, these actions and the ongoing investments should enhance our performance in key star measures and ultimately increase member satisfaction with our plans. We are actively pursuing all our options and exploring actions to mitigate the direct financial impact on payment year 2025, including through contract diversification, operating efficiency and capital deployment alternatives. We will provide updates on our action plans and progress in future engagements in advance of 2025.

Moving to Carelon. We are pleased with our momentum in the business as it continues to advance its strategy of integrated physical, behavioral, social and pharmacy services to deliver whole health affordably. Carelon services delivered particularly strong growth in operating earnings, led by the expansion of our post-acute care management solutions. We also extended our service offerings in adjacent areas, including durable medical equipment and wound care, further enhancing our customer value proposition and differentiation.

Carelon Rx continues to make significant progress towards the near-term rollout of multiple new capabilities that will enhance the affordability and experience of pharmacy for our members and Carelon Rx customers. One of these capabilities is Insure-RX, an integrated benefit for commercial pharmacy members. That compares the benefit cost for over 50 covered generic medications to our network of multiple cash discount cards then automatically applies the lowest cost at any pharmacy. The program launches early next year, and we will save our customers money while enhancing their experience. Insure-RX will also capture claim data to ensure full safety checks and maintain the integrity of our data.

We're also pleased with the integration of BioPlus, which continues to track ahead of schedule. And we expect to begin migrating specialty scripts from our legacy pharmacy platform early next year.

Finally, we remain on track to launch our advanced home delivery capability in the fourth quarter. Together, these businesses will allow us to deliver even better consumer experiences and enhance affordability while creating additional shareholder value over time.

Now I'd like to address the actions we took during the quarter to transform our cost structure and enhance our operating efficiency. With affordability of health care, a paramount concern for all of our customers and more uncertainty in the business environment heading into 2024, we took proactive and decisive action in the third quarter to increase our financial and operational flexibility and to ensure we will remain well positioned to deliver on our commitments to all of our stakeholders.

Specifically, we completed a strategic review of our operations, assets and the investments we've made over the years to identify opportunities to increase efficiency and enhance focus, all while driving greater impact from our programs at scale. This resulted in workforce and asset optimization that will make us more nimble, focused and efficient and allow us to concentrate our resources on the most promising programs while further optimizing our physical footprint. The pace of technological innovation is rapid and accelerating, and we are committed to keeping pace.

As we pivot away from some legacy projects, including those tied to systems that are being replaced with cloud-based models, we are also scaling key digital programs for greater impact. One example is Health OS, a key enabler of our strategy that is helping to change the way care providers deliver care while reducing administrative burden. Health OS is our digital platform for health that allows us to exchange data bidirectionally with providers in real time and essential to a number of our priorities, including our approach to value-based care.

We are also in the early stages of rolling out new AI capabilities and large language models that are helping us personalize member experiences and automate administrative tasks. We're excited about the possibilities of the rapid technological innovation that is underway and are committed to continuous improvement, innovation and the ongoing optimization of our processes reengineering much of what we do while delivering more personalized experiences to our members along the way.

Before I close, I'd like to note that we remain confident in our ability to close the acquisition of Blue Cross Blue Shield of Louisiana. We're actively working with local regulators and stakeholders to address any remaining questions. The deal offers tremendous value and opportunity for the people of Louisiana, including through the creation of a multibillion dollar foundation focused on improving their health and lives, and we look forward to the privilege of serving as their lifetime trusted health partner.

As you will hear from John in just a moment, the balance of our diverse set of businesses, the momentum of our enterprise strategy and the decisive actions we have taken to enhance our operating efficiency give us confidence in our ability to deliver strong growth in adjusted earnings per share in 2024.

In closing, I want to thank all of our associates around the world for their dedication and hard work. In the third quarter, we were also pleased to be named one of America's greatest workplaces by Newsweek and the #1 Best Large Workplace in Health Care by Fortune. It is the work our associates do every day on behalf of the individuals we are privileged to serve that allows us to deliver strong operating results in service of our bold purpose to improve the health of humanity. Collectively, we are fueled by passion for having a positive impact on our communities, our members and the environment.

With that, I'd like to turn the call over to John to provide more on our operating results and outlook. John?

John Edward Gallina - *Elevance Health, Inc. - Executive VP & CFO*

Thank you, Gail. And good morning to everyone on the line. As Gail mentioned earlier, we reported strong third quarter results. Given outperformance against our initial expectations year-to-date, we have increased our outlook for adjusted earnings per share in 2023 to be greater than $33, reflecting growth consistent with our long-term compound annual target of 12% to 15%.

Our outlook includes incremental investments we have planned for the fourth quarter to support growth in Medicare Advantage in 2024 and beyond. Based on our updated guidance, our 5-year compound annual growth rate in earnings per share is expected to be 16%, which makes Elevance Health the only company in our sector to have exceeded 15% over that time frame.

We ended the third quarter with 47.3 million members, an increase of 42,000 members year-over-year, driven by growth in Blue Card and ACA membership. During the quarter, medical membership declined by 664,000, driven by attrition in Medicaid due to eligibility redeterminations and a new entrant into one of our state programs in July, which resulted in a loss of approximately 140,000 Medicaid members. We are now 3 to 4 months into redeterminations of most of our states, and this enrollment in many appears to be front loaded with approximately 3/4 of those terminated from Medicaid having lost coverage for administrative reasons. We are seeing many consumers return to Medicaid after being temporarily disenrolled while others are experiencing gaps in coverage before transitioning on to ACA exchange plans. Given the patterns we have observed to date, we expect re-enrollment in the Medicaid and transitions to ACA exchange plans to accelerate.

Operating revenue in the third quarter was $42.5 billion, an increase of 7.2% over the prior year quarter. Growth was driven by rate increases to cover overall trend in our health benefits business, coupled with double-digit top line growth in Carelon Rx, driven by growth in pharmacy customers and the acquisition of BioPlus. The consolidated benefit expense ratio for the third quarter was 86.8%, an improvement of 40 basis points compared

to the third quarter of last year, driven by premium rate adjustments to cover medical cost trend and solid performance within our government business.

Now I would like to spend a moment discussing the business optimization charge we announced as part of our results this morning. As Gail mentioned earlier, we took decisive action during the quarter to position our company for long-term success by enhancing operating efficiency, refining the focus of our investments and optimizing our physical footprint. These actions will ensure we stay well positioned to provide affordable products while delivering on our commitments to all of our stakeholders.

As a result of this strategic review, we incurred a business optimization charge of approximately $700 million, comprised of write-offs and write-downs of internally developed software and related assets, severance and leases associated with optimizing our physical footprint. These actions will result in gross annual run rate operating expense savings of approximately $750 million per year, a portion of which will be reinvested in growth opportunities including Medicare Advantage and the accelerated rollout of certain digital capabilities. We are committed to doing even better, and we'll continue to evaluate opportunities to enhance operating efficiency further.

Elevance Health's adjusted operating expense ratio in the third quarter was 11.1%, a decrease of 30 basis points over the prior year quarter. However, the third quarter last year included additional out-of-period quality improvement expenses due to the accounting realignment we announced then. Excluding out-of-period quality improvement expenses in the third quarter of last year, our adjusted operating expense ratio would have been unchanged. Adjusted operating gain for the enterprise grew 12.6%, led by our health benefits business, which delivered double-digit growth as we continue to optimize premium rates and products while enhancing operating efficiency across the segment.

Operating margin for our Health Benefits business improved by 30 basis points year-over-year consistent with our expectations. Carelon also delivered a strong quarter with growth in pharmacy customers and the acquisition of BioPlus propelling Carelon Rx to 17.5% revenue growth. Carelon Rx operating earnings included investments to support the build-out of our specialty pharmacy and advanced home delivery capabilities, both of which will ramp up in the coming months.

In addition, comparisons to the third quarter of 2022 have been negatively affected by the out-of-period fee-based revenue realized in the third quarter of last year. In Carelon services, strong growth in operating earnings was driven by expansion of Carelon post-acute solutions and growth in our behavioral health business.

Turning to our balance sheet. We ended the third quarter with debt-to-capital ratio of 39.2%, in line with our expectations and consistent with our target range. During the quarter, we repurchased approximately 1.1 million shares of common stock for $480 million. Year-to-date, we repurchased 3.8 million shares of common stock for $1.7 billion, pacing ahead of our full year outlook of approximately $2 billion. We will remain opportunistic with share repurchases, especially considering the share price and recent volatility in the market. As noted in our earnings release, we ended the quarter with $5.1 billion of board-approved share repurchase authorization remaining.

We continue to maintain an appropriately prudent posture with respect to reserves. Days and claims payable stood at 48.6 days at the end of the third quarter, an increase of 2.1 days sequentially and an increase of 0.9 days year-over-year. As a reminder, we continue to expect days in claims payable to be in the low 40s range over time and anticipate normalization towards this range in the coming quarters as cycle times shortened and COVID-related claims uncertainty recedes.

Operating cash flow was approximately $2.6 billion or 2x net income in the third quarter of 2023. Excluding the impact of the business optimization charge I discussed earlier, operating cash flow would have been 1.4x net income.

Given strong performance year-to-date, we are planning to make incremental investments in the fourth quarter in Medicare Advantage marketing and retention and in capabilities and services that we expect will enhance customer satisfaction, supporting our growth in 2024 and beyond. While we are disappointed in the outcome of the recently released Star quality ratings, we remain committed to this important line of business for the long term and are exploring all options to mitigate the financial impact on 2025.

Turning to 2024. Although we are not planning to provide specific guidance on this call, I would like to review some of the tailwinds and headwinds that are known at this time, starting with our tailwinds. We continue to optimize our Health Benefits business, including by executing a multiyear margin recovery in our commercial risk-based margins to return to pre-pandemic levels and expect margin improvement will continue next year. We also anticipate improvement in Medicare earnings, driven in part by corrective actions taken in our 2024 Medicare Advantage bids to improve financial performance in Puerto Rico, where we experienced significant challenges this year.

We expect continued momentum in Carelon, including growth in Carelon services, driven by new product launches and opportunities for meaningful external growth across businesses and the ramp-up of BioPlus and the launch of Carelon advanced home delivery, both of which to supplement ongoing momentum within Carelon Rx. We also expect to enhance operating efficiency as a result of the actions we took during the third quarter, and we'll continue to look for opportunities to drive efficiency as we transform our cost structure over the long term. And we expect today's higher interest rate environment to drive growth in investment income.

Our tailwinds will be partially offset by our headwinds, which all relate to the Medicaid business where we anticipate membership attrition associated with ongoing eligibility redeterminations and the net loss of approximately 930,000 additional members associated with changes in our footprint. While Medicaid rates remain actuarially sound, we're also mindful of the risks associated with evolving risk pools, and we'll continue to monitor and manage these dynamics closely. Beyond 2024, Medicaid offers attractive long-term growth opportunities, notably in specialized populations, and we anticipate a return to growth in 2025 and beyond.

Most importantly, the balance and resilience of our diverse businesses provides confidence in our near-term outlook while the earnings power of our health benefits and Carelon divisions position us to deliver on our long-term growth commitments. At this point in time, we believe the current consensus estimate for adjusted earnings per share of approximately $37 in 2024 is appropriate, and we anticipate delivering another year of growth consistent with our long-term compound annual growth rate target next year. We look forward to providing more specific guidance on our fourth quarter earnings call.

Finally, as many of you know, this will be my last earnings call as CFO of Elevance Health. It has been a pleasure to serve this organization for more than 29 years, including the past 7 in my current role. I have been involved in 88 quarterly earnings calls since Anthem went public in 2001, including 30 of them as Chief Financial Officer. Every year has had its opportunities and challenges, and 2024 is no different. We serve our members while furthering our mission, and we'll continue to meet and exceed our shareholder commitments. The balance and resilience of our businesses has created numerous tailwinds and has allowed us to overcome various headwinds, and I'm confident we will continue to do so.

I feel fortunate to have been part of what I believe to be the best leadership team in the industry and to be leading the finance organization in an even stronger position than when I took over. I've enjoyed engaging with all of you over the years. I want to thank you for your support. I look forward to supporting Mark Kaye as he assumes the role of CFO, ensuring a smooth transition before retiring to spend more time with my family in the first quarter of next year.

With that, operator, please open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) For our first question, we'll go to the line of A.J. Rice from UBS.

A.J. Rice

John, I wish you the best in the retirement. It's been great working with you, and I really appreciate all the help over the years. I want to maybe just ask on the commercial margin improvement story and what you've been doing there. Is -- if you ex out that year this quarter, what was the underlying cost trend for you? Did you see any pockets of variance and utilization that are worth calling out. And you guys have said on the recorded or the

message so far several times that you have -- that there will be some additional benefits on the commercial margin improvement story into next year. Is there any way to size that or talk about that relative to how much gain you had this year from that repricing and the other things you're doing to improve the margin on the commercial side?

John Edward Gallina - *Elevance Health, Inc. - Executive VP & CFO*

Thank you for the kind words at the beginning. In terms of answering your question specifically though, we're certainly obviously very pleased with the performance of our Health Benefits businesses in the third quarter as well as year-to-date. As you know, we've increased margins quite significantly. And the health benefit segment margins, we guided to improve those 30 to 60 basis points year-over-year, and we're very much on track to deliver on that.

From a line of business, in particular, we're not providing specific margin information and specific detail on commercial versus Medicaid versus Medicare since we are operating this as a holistic Health Benefit segment. But we do expect continued improvement in the commercial margins into'24 as we continue to work on our strategy of ensuring that the pricing truly reflects the underlying cost structure as well as additional penetrations in the fee-based businesses what we used to call the 5:1 to 3:1 strategy. So we feel very good about where we're heading and our trajectory into 2024. So thank you for the question.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks for the question, A.J., and I'll just reiterate John's comments on commercial. I think the team has done a really nice job. As we shared, this is a multiyear journey in terms of the commercial business, and we feel like we're right on track. And the team has done a really nice job of balancing both membership retention as well as getting our margins in line where we believe they need to be. So thanks for the question.

Operator

Next, we'll go to the line of Nathan Rich from Goldman Sachs.

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

Great. And let me just echo my congratulations, John, on your retirement. I wanted to ask on the Medicare business. Could you talk about the goal for improving Star scores? Are you investing to kind of get back to the level that you are out with 65% of members in 4-star plans. And over what period are you thinking? And how should we think about the magnitude of the incremental investments planned for the fourth quarter as well as into next year? And any comment on the kind of how long it would take to reach the run rate of optimization savings, the $750 million that you talked about? It would be helpful as well.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Thanks for the question, Nathan. Let me -- I anticipate a number of questions around Star, so perhaps I'll just address that topic holistically. Improving stars for us is an enterprise priority, so I want to start with that. And we have a long-term commitment to the MA business and are committed to offering high-quality plans for seniors. But as I said in my opening comments, we're extremely disappointed on the recent results of the Stars and the decline that we saw in the number of our members in 4-star plans for payment year '25.

Just a little background, I think, it might help. We experienced some declines in the CAP survey scores, which were the most heavily weighted measures. And we were also impacted by that new CMS statistical methodology, which caused some significant increases in cut points. As you think about our performance, we improved in about half of the Star measures, but those were not enough to offset the impact of the heavily weighted measures and the higher cut points, therefore, having 3 of our largest contracts suffered in our star ratings, which you've noted.

As I shared, we have already started making those investments. And earlier this year, we were specifically addressing areas around the heightened focus for CAPS that drove the decline. One of the very specific examples is scaling the My Health Advocate model, which, again, I shared a little bit about that in my opening remarks. The model is unique and highly personalized customer service, and it's tailored specifically to help members with problems central to CAPS improvement. It's a model that we've had in place in our commercial business and has been incredibly successful.

Other areas that we saw on the data were about enhancing our core and supplemental benefits to reduce members out-of-pocket costs, which showed up in our Stars results and also simplifying how those members use our over-the-counter benefits. We bought on a journey around value-based care as we've shared with you, and we're going to continue to accelerate that and embed some of those results as well into our contracting process. And we also may take steps last year to improve the processes around clinical decision appeals, which was also an area around the higher cut points.

In terms of financial impact, we expect a reduction in 2025 quality bonus revenue of approximately $500 million after offsets from our contracting provisions. As John and I both shared, we've already aggressively begun to mitigate that headwind for '25, and we do have a number of levers at our disposal, including contract diversification, operating expense efficiencies, capital deployment and looking at targeted network and product enhancements.

Overall, we're going to continue to work on that. Our time lines have already begun on this feel. We have a very, very good line of sight to the opportunities that we have. And again, because of the diversified business model that we've talked to you about, we feel that the earnings power of our combined businesses between health benefits and Carelon allow us to continue to feel comfortable about our adjusted earnings per share growth annually of 12% to 15% over the long term. So thanks again for the question. Appreciate the opportunity to holistically address what we're doing about Stars.

Operator

Next, we'll go to the line of Lisa Gill from JPMorgan.

Calvin Alexander Sternick - *JPMorgan Chase & Co, Research Division - Analyst*

This is Cal on for Lisa. I just want to add my thanks to John wishing all the best. Switching to Medicaid. I appreciate all the color on the redeterminations and the front-loaded disenrollment trends. Can you talk about how membership is trending relative to what you expected earlier this year and how acuity mix is trending? And then related on the commercial side, how membership growth is tracking in the employer group and individual businesses. Are you guys getting the growth you anticipated? And is there anything to call out on the margin side as you think about this year into 2024?

John Edward Gallina - *Elevance Health, Inc. - Executive VP & CFO*

Thank you for the question, Cal, and certainly appreciate all the commentary. But first of all, on Medicaid, the Medicaid disenrollment, as we said, has been very much front loaded. And in terms of how that compares to our expectations, our expectations were that it would have been more normalized over a 12- to 14-month process. We -- what we are seeing is that there's administrative churn and that a lot of people are losing Medicaid coverage temporarily. And then they're coming back on. We're reenrolling folks 30, 60, 90 days after they were disenrolled. And that was -- that dynamic was not part of the original thought process, but it's certainly part of the reality.

I'd like to say, September 30 or December 31 for that matter is just going to be one point in time over a 12- to 14-month process. What we have not seen and maybe the most important element is that, at the beginning of the year, when we discussed that we think that we're going to retain about 40% to 45% of all Medicaid members who received coverage during the PHE, we still believe that is a very good estimate. And by the time the dust settles in the third quarter of 2024, we feel good about that estimate. It's just going to be a little bumpier or rockier along the way because of the gaps in coverage and because of the administrative churn.

And on the commercial side, we're actually seeing really excellent growth in the individual ACA. Once that redeterminations began in a particular state, the level of applications on the ACA products were up 3x the amount that they were prior to that. And so that really does point to the fact that we do have the catcher's mitt in action.

The employer-sponsored side, that's actually going maybe a little bit less than we had anticipated. So individual ACA is going a little bit faster. Employers sponsored a little bit slower. But all in, we really do believe that by the time we get through this entire process, which won't be completed until sometime in the third quarter of 2024, that the estimates that we provided at the beginning of the year will prove to be pretty good estimates. So hopefully, that helps.

Operator

Next, we'll go to the line of Stephen Baxter from Wells Fargo.

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

Wanted to follow up on the Medicaid redeterminations question there. So I appreciate all that commentary you just made. Would it be fair to say that at this point in part driven by the fact that you've got seemingly good and actuarially sound rate updates from your states that you haven't really seen all that much normalization of your margins in 2023? I believe you came into the year thinking that you performed in 2022 above your long-term targeted range, and there might be some pressure. I would love to just get an update on how that's performed in 2023 and how you're thinking or potentially considering that in your comments on 2024.

John Edward Gallina - *Elevance Health, Inc. - Executive VP & CFO*

Yes, sure. Thank you very much for that question. And actually, I think Cal did ask about acuity as well. So hopefully, I'll address both of those here with this answer. Medicaid continues to be doing very well, very much in line with our expectations and in line with what we saw coming. The one thing that I will reinforce is that in the rating formulas in the future or currently now is an acuity factor that's supposed to take changes in acuity into consideration. That factor was not in place in 2019. So comparisons to 2019 really aren't all that relevant at this point in time for that purpose.

What we've seen thus far though is very little change in the overall acuity of the book. We are taking a very close look at that. And as I stated in my prepared comments, we're going to be monitoring that extremely closely and working with our states. So I'm very happy to report that all of the renewals that we've had with the discussions we've had with the states thus far, we have been provided actuarially sound rates. And we believe with actuarially sound rates, we can continue to deliver on Medicaid consistent with how we have in the past, providing a lot of benefits to the beneficiaries and providing returns to the shareholders. So thank you.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks, John. And I think as -- just to put a sort of summary on that, we feel we've got great visibility into the rest of this year. And the discussions around '24 have been incredibly productive with about 50% of our premiums with good visibility there. So we think that those conversations are going well, and things are tracking according to expectations. So thanks for the question.

Operator

Next, we'll go to the line of Ben Hendrix from RBC Capital Markets.

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

I just also want to reiterate congratulations to John and thank you for all the help. just wanted to circle up with a quick follow-up on MA. Appreciate all the questions on My Health Advocate and efforts there. I just wanted to know if there's any early thoughts on how much of the headwind you can mitigate with contract diversification and then kind of what the time line is for getting all those approvals at the state level to carry that forward.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks for the question, Ben. As we think about that, as I said, we've got a number of levers at our disposal. And so I would focus on that. But in terms of contract diversification, about 1/3 of the members affected were in the group contracts. So we'll look at moving those potentially to a 4-star contract. But again, I just want to reiterate, it's just one lever in our toolbox. And so we're not just looking at that, but we're looking across all of the things to have a mitigation for 2025.

So thanks again for the question. And again, a lot happening in our enterprise around the efforts there to make sure that we remediate and stay very focused. This is an enterprise priority for us.

Operator

Next, we'll go to the line of Kevin Fischbeck from Bank of America.

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

Great. And I was to add to my congratulations to John as well. I guess as far as the cost cutting, this cost cut was quite large. And I guess I just want to get a little more color at exactly kind of what's driving this. It sounds like this was all before your new stars was going to be off for '25, because it sounds like it was more a '24 issue. I think in the comments, you said something on the line that it's going to help you deliver lower cost to customers, but also addresses some of the uncertainty in 2024. So I just want a little more color on that. How much of this is going to improve benefits in MA versus, I think you made technology investments? Just a little more rationale for the move why it's so big. And then if the -- if you're doing it this move now, how do you think about your ability to find significant savings to offset Stars 2025?

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks for the question, Kevin. I think -- let me put this in a little perspective because it's important to note, we're always evaluating our cost structure. And as we headed into 2024, we took very proactive and decisive action in the third quarter. We wanted a couple of things. One, increase our financial and operational flexibility and also ensure that we're positioned to deliver on our commitments to stakeholders. So if you look at the charge in total, I mean it really is kind of focused in 3 areas of cost management. And I think it's prudent to continue to always look at your cost structure, something we've been doing, obviously, as we've been looking to manage that.

And let me go through the 3 pieces because I think it's important. First, as you know and we've talked about quite a bit on these calls, we've been investing over the past several years in modernizing our infrastructure, particularly around digital capabilities and migrating a lot of our applications to the cloud, consolidating our systems and our data and now most recently, use cases on using AI to drive greater efficiencies. The pace of technological innovation has changed, and it continues to accelerate. And again, as I said, we're committed to deploying those responsibly quickly in our company. So what you're seeing in that first bucket is the write-down of some of those legacy processes that have now been replaced with our support -- that support our long-term goals with digital and AI and other things. And we've gone through that first phase that we've been talking about over the last several years on consolidation, data aggregation, et cetera.

The second adjustments were really to our workforce. And that, again, last year, we aligned our structure on benefits and services. This gave us an opportunity to look at redundancies across our business and our processes and eliminate handoffs, streamlined, very focused on ensuring that members because of our large benefit businesses can move between those businesses. It's an integral part of our strategy. And so that's been an

important part of streamlining our work processes, simplifying our member experiences. And so as you think about the investments that we've been making in technology, particularly our front door applications and things that automate some of our work, this was an opportunity for us to make sure that we had the right scaling of our workforce. And again, in the bigger scheme, these are not significant numbers. But again, I think it's really important that we constantly look at our cost structure.

And then the last part is we went to a hybrid work environment. We've been evaluating the size and locations of our work sites, and we took the opportunity to further optimize those to make sure that we were located in the right places and had the right footprint.

So you think about all those, it's an approximately $700 million of charges, and it results in a run rate of about $750 million. Again, as John said, it doesn't all drop to the bottom line, but that we think is important to support our long-term growth in our enterprise strategy. So that gives you a bit of a sense of how we thought about these as an ongoing opportunity to continue to optimize our cost, which we think is important for affordability in health care. So thanks very much for the question.

Operator

Next, we'll go to the line of Sarah James from Cantor Fitzgerald.

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

Echo my congratulations to John. I was hoping that you guys could give a little bit more context around the recapture rate of the terminated Medicaid lives. So are you seeing recapture within Medicaid from the appeal process yet?

And then on the ACA side, how do you think about the 30% recapture maturing into '24 with your members, but then also potentially there's more people looking for ACA plans in '24?

John Edward Gallina - *Elevance Health, Inc. - Executive VP & CFO*

Thank you for the question, Sarah. So in terms of the Medicaid redeterminations, as I stated, we're 3 to 4 months into the process. And it's a little early to have definitive in very specific data points, but we do have certainly the bias. We've seen 10% to 20% of the members who lost coverage in Medicaid in June reenrolled with us in the third quarter. So we certainly expect trends like that to continue. That's just one data point and certainly, there's more time. But there are gaps in coverage.

And then on the individual ACA, we are seeing by the time that folks leave Medicaid. There's typically a couple of month gap before they become enrolled in ACA plan. So some of the membership disenrollment is temporary, and there's gaps in coverage. So we've seen that throughout. But we think we have a great opportunity in our 14 Blue states. You look at the number of members that were added to Medicaid in our 14 Blue states, that was about 8 million people across all 14 states. About 1.5 million of those were enrolled in Elevance Health Medicaid plans, which means that those other 6.5 million that went to a different carrier, if that different carrier is able to retain 40% to 45% of those Medicaid similar to us, which I think is a reasonable expectation, that means that over half of the 6.5 million are in play. And we have leading market share in virtually every market we operate in, both in employer-sponsored as well as very strong in the ACA products.

And so we do believe that you will see an acceleration of individual ACA membership in the early '24 and mid-'24 for Elevance Health. So hopefully, that answers your questions. Thank you for the question.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks, John. And Sarah, I think just to sort of put a bow on this. I think it's really important just to frame it, almost 75% are administrative disenrollments and then over almost 37% are children under 18. So those are 2 areas, obviously, we're intensely focused on. And there's a timing

issue associated with this. So there's some delays in coverage and some coverage gaps, and we've been working really closely with our states. But as John said, we are seeing some encouraging signs where that 30% or more of our Medicaid members who are terminated prior to the end of June are now returning and retaining coverage with Elevance.

So we expect that re-enrollment to accelerate in the coming quarters. So I think that's important to keep in mind as we're all working through this process and certainly, the states are working through this process. And we have been continuing to adapt how we get to these members, particularly the ones that were disenrolled for administrative reasons. So again, we feel pretty comfortable with the numbers that we shared and the guidelines we showed, and we are seeing pickup certainly in the individual business as this progresses. So thanks again for the question.

Operator

Next, we'll go to the line of Michael Ha from Morgan Stanley.

Michael Ha

Congrats to John as well. I wanted to ask a quick question first regarding BioPlus. I wanted to confirm, did you mention you're going to start migrating specialty scripts away from your legacy platform early next year? Would that imply you've made the decision to in-source your specialty drug spend away from CBS?

And then my real question, just regarding MA and Star ratings, in terms of the improvement efforts for CAP specifically, how much of the overall underperformance would you attribute to the providers strictly? And how can you fix those results for that without actually having ownership of providers? I mean how can you effectively drive your provider network to make the necessary changes to improve your results? Curious what the plan is there.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Thanks for the question, Michael. I'll have Pete start, and then I'll address your question on MA.

Peter David Haytaian - *Elevance Health, Inc. - Executive VP and President of Carelon & CarelonRx*

Thanks for the question, Michael. Yes, to answer your question directly, we are beginning the migration to BioPlus starting January 1. And again, just to reiterate, we've been very, very focused on the last year with regard to implementation and integration of BioPlus as it relates to our specialty strategy. A lot of the focus this year has been building the infrastructure and the team, so that we have the appropriate scale and capacity to take on the Elevance Health volume. And we feel very good about that. As Gail noted in her prepared remarks, we are accelerating the time line in that regard, and we are moving forward with that for January 1. And again, this is all a part of our strategy in pharmacy, just to reiterate, and that is to in-source the strategic levers that matter. Specialty pharmacy is very critical to that as well as what we're doing in advanced home delivery. So again, excited about that. And yes, it is launching January 1.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. And to the second part of your question is we have delved in and really looked deeply at sort of what the drivers -- especially around the 3 contracts and sort of what the cut points were. I guess I would say there's a couple of things. One has been easier navigation for our members. So I would not say it's because of ownership or lack of ownership, but I will address sort of value-based care. Remember, this was measurement around year '22. We've made significant progress around moving a lot of our contracts to value-based care and embedding that into the way we do it. We've also worked closely with aggregators and have been building, quite frankly, the numbers in that. So we do feel that our strategies are intensely focused, and our health navigator will significantly help them.

The other area, quite frankly, around the cut points that impacted us was appeals and grievances in some of our processes back in 2022. Those were very high-performing contracts in the past, and the cut points while still good performance for us, we're below the cut point. So I think those are very specific things that we can address.

I want to take a moment, though, I think, to talk about where we are in value-based care because I think it is important. It's a Medicare Advantage, an area that we've been intensely focused on. So I mentioned on the primary care side, we've been working with a number of aggregators, plus increasing the amount of value-based care, but more importantly, embedding in those contracts, quality and outcome measures as well as access and service. And I think those will have it -- continued, I guess, have an important impact on those.

The other opportunity that we have is around specialty care, and we have been doing quite a bit of work on aggregation of specialty care and particularly carving in high complex areas on specialty medical spend. That's an area where we see significant opportunities and don't see that as a really mature part of the market today.

For example, Carelon is launching in January in oncology, specialized care model with our affiliated health plans, and it's allowing us also to more broadly commercialize that opportunity. We also see opportunities in musculoskeletal, renal and more. And I think this is a really differentiated focus because as we think about where members are very focused on access is around specialty care, and I think we have a unique opportunity from both our innovation, our technology and the clinical expertise we offer to run that through Carelon with our health benefits, particularly in Medicare, but also across all of our lines of business. And that's going to be an important strength for us, and that's an area that I think in the specialty enablement will help our Medicare Advantage stars, but also help our patients get better access to that care. So that's -- we think it's a differentiator.

But overall, your question, I think we're very focused on the areas that drove some of the areas within those 3 contracts, and we feel we have a very good line of sight to what they were. And a lot of them were easier navigation for our members and making sure that it was a much more personalized experience than we've had in the past. And then again, ensuring that our supplemental benefits and over the counter are simpler and easier to use, and we shared a little bit of that. And we made those changes actually in our bids over the last couple of years. So thanks very much for the question, Michael.

Operator

Next, we'll go to the line of Josh Raskin from Nephron Research.

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

I'll add my congrats for 88 quarters for John as well. My question, can you speak to the strategy of how Carelon and Benefits segments aimed to really work together over time? I'm specifically interested in how you tie sort of the various companies within Carelon together and then also on that care delivery side as part of the answer.

And then lastly, are there certain any capabilities -- certain capabilities that you think are missing or would be helpful for Elevance in terms of putting together that totality of strategy?

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Yes. Thanks for that question, Josh. We'd love to share more about our strategy. I'm going to have Pete Haytaian talk about it. As you know, he leads that part of our business.

Peter David Haytaian - *Elevance Health, Inc. - Executive VP and President of Carelon & CarelonRx*

Yes. No, thanks for the question. I really appreciate it. I think it is a good opportunity to talk about our strategy holistically. As Gail mentioned in her prepared remarks, we talk about whole health and integrated care and driving affordability. But I really want to tag off of what Gail just talked about because I really do believe it's what we're focused on and differentiating ourselves on, and that is looking at high cost, high spend areas at health care. We face off with our health plan partners. We identify those areas, specialty care as a tremendous opportunity and a real differentiator. Gail mentioned some areas that are critically important to us as we move forward, and this is across all lines of business, not one particular line of business. But when you think about high-spend areas like oncology, like MSK, like renal, we have a wonderful opportunity to manage the member holistically and take full risk on those members.

Now importantly, that's -- it's a big part of our strategy in terms of assuming full risk on those categories, driving earnings through Carelon, our unregulated entity, and also focusing on areas and profit pools that are growing where we have a wonderful commercialization opportunity. And how this all plays together is we face off with Elevance Health. We identify these areas. We drive capitated full risk in many of these instances, and then we deploy those capabilities externally. This is really playing through in a nice way, and we're seeing that play through in terms of our growth trajectory.

To just, again, reiterate what Gail said, in January of this year, we're going to be launching an oncology program at full risk. We are also looking at taking full risk on the seriously mentally ill in behavioral health where we're not only managing the behavioral health, but the physical health side. And this is all the type of thing that is playing through into our external pipeline, which we're seeing grow nicely.

So I really appreciate the question, Josh. I think -- oh yes, and by the way, you did ask questions around additional capabilities. I would say that M&A also is an important part of our strategy as we move forward. And when you think about these highly specialized areas of care, we're not naive to think that we have the capabilities internally to handle all of it. When you think about MSK, when you think about renal, even what we're doing around the seriously mentally ill, we will be looking to not only partnerships but acquisitions that can help us in that regard.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Thanks, Pete, and thanks for the question. And I think if I just summarize everything Pete said, we're really working in Carelon across kind of 4 major areas. Obviously, pharmacy with Carelon Rx and then three pillars inside of our Carelon services business, care delivery, our insights and our behavioral health. And all of those come together in all of Pete said. And we have a great opportunity to provide greater certainty and cost management to our owned health businesses, but externally commercialize that and seen a lot of momentum going into '24 on that, prove it on ourselves and then show the market the capabilities, particularly around the Blue system. So thanks again for the question, Josh, and this will be our last question.

Operator

And for our final question, we'll go to the line of Justin Lake from Wolfe Research.

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

Thanks for squeezing me in, and I'll ask there my thanks to John for everything over the years. Really appreciate it, bud. Along those lines, Gail, maybe you can give us a little color around the CFO search and what you expect Mark to bring to the organization. And then just curious if you have any early views on 2024 Medicare Advantage membership growth, both for Elevance and the market overall?

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Well, thanks for the question, Justin. And first of all, I will also offer my appreciation to John for his guidance and his counsel and honestly, our partnership over the time that I have been CEO. John and Mark has been here now for about a month. We're excited about having Mark Kaye join

us. As you know, he was the CFO of Moody's. Mark brings -- he's an actuary by training, brings an incredible insight to our business. He and John have been working hand-in-hand on the transition, and John will be continuing as an adviser to me through the first quarter, as you heard in his opening remarks.

I think we're at an incredible time in our business. We have great growth. We have a very diversified business, and I'm excited about Mark joining our team and excited about the whole team. And thank John, we will all miss him, but he deserves time with his family and an opportunity to do things and work on his golf game, as you know, Justin. So from that -- and I'm going to ask Felicia to comment a little bit about Medicare Advantage. As you know, AEP has just started. So it's really very early in days, so maybe Felicia can share a few comments about her thoughts on what we expect.

Felicia Farr Norwood - *Elevance Health, Inc. - Executive VP & President of Government Health Benefits*

Justin, thank you. We are actually very excited about AEP. As Gail referenced, we are only 3 days in, but we're actually very pleased with the response we have from our brokers regarding the competitive positioning of our benefits, and we believe that we will be able to grow membership above the market excluding the strategic decisions that we made around targeted market exits. So I want to point out that we made the very intentional and discrete decision to leave some markets that have been underperforming for us for some period of time. Strategically, it was the right thing to do so that we can make sure we are focused on those markets where we have an opportunity to be very successful, deliver strong benefits for the members that we're privileged to serve.

So as we think about where we are today, we feel good about our positioning. As I said, we're very early in terms of where we are. But we believe as we head into 2024, we're going to be able to deliver solid growth. As I said, I believe that will be above the overall market rate based on where we're positioned. So thank you very much for the question.

Gail Koziara Boudreaux - *Elevance Health, Inc. - President, CEO & Director*

Well, thank you, Felicia. And thank you to all of you on the line for your continued support and for joining us. Through a steadfast focus on whole health and our diverse and expanding suite of products and solutions, we will continue to meet the needs of clients, consumers and the communities we serve, advancing our strategy of becoming a lifetime trusted health partner while delivering on our commitments to all of our stakeholders. Thank you for your interest in Elevance Health, and have a great rest of the week.

Operator

Ladies and gentlemen, a recording of this conference will be available for replay after 11:00 a.m. today through November 17, 2023. You may access the replay system at any time by dialing (866) 405-7293, and international participants can dial (203) 369-0605. This concludes our conference for today. Thank you for your participation and for using Verizon conferencing. You may now disconnect.
