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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Elevance Health First 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 First Quarter 2024 Earning 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; Mark Kaye, our CFO; and Pete Haytaian, President of Carelon; Morgan Kendrick, President of our Commercial 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, recent progress against our strategic initiatives and our updated outlook for the year. Mark 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*

Thank you, Steve, and good morning, everyone. We appreciate you joining today's earnings call. I'm pleased to report that Elevance Health delivered first quarter GAAP earnings per share of $9.59 and adjusted diluted earnings per share of $10.64, reflecting growth of 12.5%. These results reflect disciplined execution of our strategic initiatives during a dynamic time for our industry. Given the solid start to the year, we have increased our guidance for adjusted earnings per share by $0.10 to be greater than $37.20. We are making significant progress on our enterprise strategy in 2024 to accelerate capabilities and services, invest in high-growth opportunities and optimize our Health Benefits business.

On Monday, we announced the next step in our journey to expand access to high-quality patient-centered value-based care in our local market. After years of experience working closely with care providers to advance value-based care, we are confident that our hyper local approach, which aligns the right incentives, real-time patient information and clinical decision support tools, delivers better health outcomes, improve consumer and provider experience and greater affordability.

Accordingly, we entered into an agreement to form a strategic partnership with Clayton, Dubilier & Rice to build a payer-agnostic advanced primary care and physician enablement business, serving consumers across commercial, Medicare and Medicaid health plans, consistent with the diversity of our own medical membership. Upon formation, the combined company will serve nearly 1 million consumers. The new venture will bring together the strength of 3 innovative care provider entities, including certain care delivery and enablement assets of Carelon Health.

Importantly, we have worked closely with these companies and their management teams and are confident in the value they deliver for our Medicare, Medicaid and commercial health plan members and employers. We're excited to collaborate with CD&R and a broad range of care provider partners to accelerate innovation, enhance health care experiences and improve health outcomes for consumers. The collaborative development of the business will advance our enterprise strategy by accelerating the provision of value-based care for our members and consumers more broadly, with our Carelon businesses providing capabilities to integrate and personalize the care delivered. In time, Elevance Health will have full ownership of what we expect will be a leading platform for value-based care delivery and physician enablement at scale across commercial group, ACA, Medicare and Medicaid health plans, advancing our role as a lifetime trusted health partner for the consumers we are privileged to serve.

In the first quarter, we made tangible progress on our strategic initiatives, notably in Carelon, where we continue to scale our flywheel for enterprise growth. CarelonRx closed its acquisition of Paragon Healthcare, a leading provider of infusion services. We are looking forward to expanding its geographic reach and therapeutic coverage to serve more consumers and Elevance Health members for years to come. As CarelonRx furthers our enterprise commitment to address the whole health needs of our members, notably those with chronic and complex conditions, we are accelerating the build-out of our own specialty pharmacy.

For example, we recently entered into an agreement to acquire Kroger Specialty Pharmacy business, the sixth largest specialty pharmacy in the country. The acquisition will bolster the growth of our existing pharmacy and infusion businesses, while increasing CarelonRx' access to limited distribution drugs. Carelon Services is also up to a strong start this year as we implemented and were awarded multiple new contracts, a testament to the value Carelon Services provides. For instance, Carelon Behavioral Health was selected by the Maryland Department of Health to provide behavioral health management services to more than 1.7 million Medicaid members starting in 2025.

And in California, our team will partner with the public school system to expand behavioral health management services for students later this year. This initiative represents a major step forward in addressing the critical need for mental health support in educational settings and demonstrates our commitment to improving the health and well-being of our communities. Momentum with external clients is building and underscores the value Carelon Services is creating for health plan customers to better consumer experiences and improved affordability. Our Health Benefits business is similarly off to a solid start. Commercial margin continues to recover from pandemic era lows, and we are enjoying momentum in membership growth, notably in our individual ACA plans and among large self-insured employers.

Existing clients are demonstrating their confidence in our offerings by consolidating their business with us after years of offering our solutions side-by-side with those of our competitors. In our Medicaid business, we were pleased to be selected in Florida and Virginia to serve beneficiaries across traditional and complex populations statewide, including those with serious mental illness in Florida, and Sole-Source Foster Care in Virginia. These awards and their pull-through opportunities for Carelon Services underscore the distinct value Elevance Health delivers. In the first quarter, our Medicaid business performed in line with our expectations. We estimate that nearly 90% of our members have had their eligibility redetermined.

Further, our team continues to work tirelessly to maximize access to care for Medicaid members subject to eligibility redetermination, helping them to understand their options in the face of ongoing logistical and operational challenges. Holistically, we are proud of the work we have done in contacting more than 4.5 million Medicaid beneficiaries through our omnichannel approach. Nonetheless, a majority of members who have lost coverage for administrative reasons have not yet returned. We're seeing a gradual increase in Medicaid reenrollment and anticipate continued upticks in rejoiner rates as more Medicaid beneficiaries recognize their need to reenroll, aligned with the trends that we have observed in recent months.

Turning to Medicare. We were pleased to announce last month that CMS updated the Star scores for 4 of our contracts, which increased the percentage of our members in 4-star or higher-rated contracts to nearly 50%, up from 34%. While this will improve our Star quality bonus revenue in 2025, our goal is to have our Star quality ratings at the high end of all plans in our local markets, which will be a multiyear journey. Funding for Medicare in 2025 will be challenging for the entire industry. We are disappointed that CMS has decided to cut Medicare Advantage rates for the second consecutive year, which will negatively impact seniors, notably, those at the lower end of the income spectrum who rely on the program for their health and well-being.

While we remain committed to serving seniors through plan offerings that focus on their unique needs, we will also continue to demonstrate discipline in our Medicare Advantage bids, seeking to balance growth and margin while continuing to deliver exceptional value for seniors. Across the enterprise, our focus on delivering whole health for the consumers we are privileged to serve remains steadfast. We recently released our 2023 Advancing Health Together Progress Report, which underscores the strides we are making through value-based care. The report showcases examples of our success, facilitated by the unique partnerships that we've created with care providers across the health care ecosystem. I'd like to highlight a particular achievement that underscores our innovative approach to improving quality and value in health care.

Recently, Elevance Health was honored by the NCQA with its innovation award featuring quality accelerators in health care for leading-edge strategies that improve quality and value, specifically for our obstetric specialty provider enablement program. The impact of these value-based partnerships and clinical interventions has led to consistent improvements in health outcomes and costs, including reducing preterm birth rates by 12% and low birthweight babies by 20%, all while improving access to timely prenatal care and postpartum follow-up. For those interested in learning more about these transformative initiatives and other examples of our progress, I encourage you to visit our Advancing Health Together website.

In closing, I want to extend my deep gratitude to our 100,000 associates who embody our purpose of improving the health of humanity through their tireless commitment. It's also heartening to see their efforts recognized externally. We were honored to be named to Fortune Magazine's 100 Best Companies to Work For list for the fourth year in a row. We were also included in their world's most admired companies and America's most innovative companies list.

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

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

Thank you, Gail. As you heard earlier, our first quarter results reflect solid performance under a dynamic operating environment. We ended March with 46.2 million members, reflecting Medicaid attrition partially offset by ongoing momentum in our commercial business. During the quarter, we added nearly 400,000 commercial fee-based members, driven by strong retention and a successful national account selling season and over 200,000 individual ACA members given our attractive product positioning and coverage transitions away from Medicaid. Medicare Advantage membership declined slightly, as expected, given select market exits and the collective actions we continue to take to establish a strong foundation for profitable and sustainable growth over the long term.

Operating revenue for the quarter was $42.3 billion, in line with our expectations. The consolidated benefit expense ratio of 85.6% improved 20 basis points year-over-year due to disciplined premium rate adjustments to reflect medical cost trends and the ongoing recovery of commercial margins from pandemic era lows. The adjusted operating expense ratio was 11.4%, consistent with the first quarter of 2023, indicative of our commitment to disciplined expense management and investment prioritization. Solid performance and growth in operating gains for both our Health Benefits and Carelon segments of $138 million and $72 million, respectively, led to growth in consolidated adjusted operating gains of over 7%.

Carelon Services had a particularly strong start to the year, with revenue and operating earnings growth driven by risk-based service line expansions and effective cost management, especially in our Carelon Insights and Carelon Behavioral Health businesses, further accelerating our enterprise flywheel or growth. Operating cash flow in the first quarter was $2 billion or approximately 0.9x net income. With respect to the balance sheet, we ended the quarter with a debt-to-capital ratio of 39.4%, in line with our target range preserving ongoing capital allocation flexibility. We repurchased 1.1 million shares of common stock for approximately $566 million during the quarter, underscoring our confidence in the intrinsic value of our shares and the long-term value proposition.

We maintained our prudent and consistent approach to reserving. Days in claims payable stood at 49 days as of March 31, up 3 days from the prior year quarter. This increase was largely driven by higher reserves associated with slower claims receipts due to an industry-wide disruption that impacted a major claims clearinghouse. As a reminder, we expect our days in claims payable to be in the low 40s range long term. I'd also like to take a moment to provide additional color on our strategic partnership with Clayton, Dubilier & Rice. We are excited to partner with CD&R to scale what will be a best-in-class payer-agnostic advanced care delivery and enablement platform catering to the unique needs of consumers regardless of their form of coverage.

This collaboration will allow us to advance our local oriented approach to care delivery based on the unique needs of the communities, consumers and employers we are privileged to serve. At the onset, Elevance Health will hold a significant minority position in the combined business with a clear path to first majority and then full ownership in approximately 5 years. The formation of the strategic partnership includes our capital contribution in the form of cash and our equity interest in certain care delivery and enablement assets of Carelon Health as well as the conveyance from CD&R of our Apree health and Millennium Physician Group and is subject to customary regulatory approvals.

Overall, we are pleased with our first quarter performance and a solid start to the year, momentum in our Health Benefits and Carelon businesses. And the balance and resilience of our enterprise underscores our confidence in delivering another year of growth in adjusted diluted earnings per share consistent with our long-term compound annual growth rate of at least 12%. As we look forward to the rest of 2024, our focus will remain on successfully executing our strategy as we accelerate capabilities and services, invest in high-growth opportunities and optimize our health benefits business.

And with that, operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) For our first question, we'll go to the line of Lance Wilkes from Bernstein.

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

Let me ask a little bit about the value-based care strategy and the execution, that's obviously a really big step forward. Could you talk a little bit about kind of the vision and scope of this? Is this going to be more focused on enablement? Or in particular markets, is practice ownership going to be important? And then maybe if you can kind of color in the picture a little bit as far as leadership, names, which Carelon assets are going to be contributed. And near term, do you see -- which areas of leverage across the membership base of Elevance do you see this being able to penetrate most effectively?

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

Well, great. Thanks so much for the question, Lance. First, as I shared on in my opening comments, we're very excited about this partnership with CD&R because it is very much the next step in our journey to bring value-based care to more consumers, specifically about partnering closely with care providers and we see it as absolutely consistent, driving greater risk adoption and advancing our specialty enablement strategy as well. So it's very much a first step there. And as you said in your question, this aligns very closely with our strategy and our broad partnership focus to work directly with care providers in our local markets. And our goal again remains to increase more downside risk sharing in our value-based arrangements. I think, to take a step back, what makes this approach unique is that we're enabling value-based care across all lines of business.

So as I shared, the combined company is going to be payer agnostic, and it's focused on enabling advanced primary care locally. And from the get-go, it's going to serve nearly 1 million consumers, and that's going to be across our commercial, Medicare and Medicaid health plans upon formation. Another thing I think is important is that it provides the opportunity to pull through Carelon Services to support those patients and accelerate that specialty enablement for complex and chronic patients. We have been working with these management teams and these assets for some time, and feel very confident about the alignment of our goals to serve as a lifetime trusted health partner. The goal gets back again to focusing on whole health, the needs of consumers driving greater affordability and fundamentally a differentiated consumer experience.

A few things about the partnership, too, and, again, what makes it different for patients? They're going to have access to integrated teams. We're looking at personalized navigation, expanded digital assets and specialized services. The primary care model is going to be built to be very distinctive, including community practices, purpose-built clinics, high-risk clinics and digitally enabled care model. So you can see it's a fairly comprehensive approach. And the last thing I'd say is that employers in market have not historically had access to a lot of these capabilities.

And we have seen through the work that we're already doing that this dedicated primary care capacity that integrates the clinical and benefits navigation with their specific health and wellness strategies is truly differentiating. So again, this is being purpose built to work across all of the aspects of Medicare, Medicare, commercial, not just a single business. So very much excited. We see this as an opportunity to accelerate innovation in the space and improve health care outcomes and consumer experiences. So thanks very much for the question.

Operator

Next, we'll go to the line of A.J. Rice from UBS.

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

I appreciate Mark's comments about the buildup and a little bit on days in claims payable, but just maybe to flush out a little bit more on the impact of the Change cyberattack on results. Do you have a sense as to what percentage of your claims that you normally see in the first quarter may still be out there? Do you feel like you've got a good handle on that? And anything when you address that in terms of your normal IBNR and maybe you've got a significantly higher level of IBNR because you're allowing for the Change and if you can break out what you're actually seeing a little bit on cost trends versus needing to sort of provision for the unknowns of the Change cyberattack.

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

Thanks for the question, A.J. Let me maybe provide some broad-based comments and then I'll turn it over to Mark to provide a little more specificity on your questions.

I want to say, first and foremost, I'm really proud of our teams on how they responded to this issue that occurred with Change quickly and effectively, first, to protect our members and their data and also help our care providers maintain their operations and cash flow. Importantly, I think it's important to note that from a perspective, we were not as significantly impacted by this, and we are back to normal operations in terms of claims flow. Importantly, another thing that's really important to understand is our prior authorization, provider payments and pharmacy claims were not materially impacted as well because they don't go through Change. We don't use Change significantly for those.

So with that, I'll turn it over to Mark to provide a little more comments. But I think framing it overall, we feel that our teams acted quite quickly and really proud of our ability to work in the ecosystem to help support them.

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

As you just heard from Gail, we acted quite responsibly to sever our network connections to Change Healthcare and to protect the data of both our members and providers. While we initially observed a 15% to 20% reduction in the daily volume of electronic data receipts from providers, most of which are claims related. In recent weeks, our extensive efforts have led to a significant catch-up in outstanding claim volumes. And for the quarter, we are effectively caught up on claims receipts and are now working to complete all necessary claims adjudication and processing activities.

As such, it's part of the normal reserving practices, we've reflected the appropriate impact of the industry-wide disruption related to Change Healthcare in the reserves we reported for our first quarter financials and that ensures both consistency with historical practice and prudence. And then to your specific question, the impact here was to increase our sequential days in claims payable quarterly result by approximately 1.7 days.

Operator

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

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

I wanted to get back to the partnership with CD&R. And specifically, what alternatives did you evaluate and consider before coming to this arrangement? I think in the past, you were stressing more, and I've heard it today as well that focus on specialty care. So how does that fit in and sort of get bolted on top of this? And maybe where does this fit into your longer-term national approach? And then how important was it that you could serve multiple memberships not just Medicare Advantage.

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

Yes. Thanks for the question, Josh, because I think it very much aligns to the strategy that we've laid out. I guess, first and foremost, it's payer agnostic, and it was really important. We've always said that our goal, given the diversity of our business mix is to serve all members across all business lines. Given the depth and density of our membership in our local markets, that is very important. We had a partnership already working with many of these assets. So as I said, we know the membership -- we know the leadership teams. We know the value that can be created. And so we have been working with them and feel quite good about what we can create. This is payer agnostic, which we also think is very important. And again, this will help us continue through having a focus on advanced primary care, it's still very much focused on our chronic patients and complex patients. And we are still building specialty care enablement, which is, again, another very important component of what we're trying to probe through.

So I think from that value-based care across all lines of business, a critical part of our strategy, very consistent, driving value-based care, continuing to drive much more downside risk, which means that we needed strong enablement capabilities to help practices work their way through that. We know that it takes time. It is also a technology-driven model. So one of the nice things about this partnership is that there are embedded technology assets to digitally enable care as well. And then we have a focus on patient access and experience in the adoption of next-generation models. So again, consistent with the strategy that we've had over the last several years, not really a diversion, I think, from that. And I think the timing for us was right because we have been experimenting with multiple models and have a lot of experience in the space right now.

Operator

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

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

Just another question on the CD&R partnership. To what extent are these primary care platforms taking risk currently? Is that something that we will need to see develop as we kind of get more of these digital enablement abilities from Carelon? Just wanted to see over the 5-year horizon to full ownership, if we can expect to kind of get the full capitation on these platforms over that time period?

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

Thanks, Ben. I'm going to have Pete probably provide a lot more context. But just quickly, about 1/3 of the membership is under risk arrangement now. So with that, Pete, why don't you give a little more color into the relationship and how we see it evolve.

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

That's great. Thanks for the question, Ben. And I'll give you a little bit more color on the assets and the capabilities. They really all have the distinct strengths. We see great opportunities, quite frankly, to cross-pollinate. When you think about MPG, to your question on risk, they really are a leader in managing Medicare and commercial risk. And they've also got a very strong chassis, I think, for future growth and a proven model in that regard in terms of acquiring provider practices. So very strong at managing risk and a lot of capabilities in that regard. What's really interesting about Apree, and Gail referenced this is, they've got a differentiating technology and navigation capabilities with a real strong focus on the commercial business. So a really nice entry point for us.

We've been working on relationships already in this regard. And I'm really excited about that because we, obviously, as a company, have a really strong commercial footprint, a really nice entry point for us. And then, of course, Carelon Health advanced primary care, which is a leader in managing the complex and the chronic and largely takes risk today. We see a tremendous opportunity in a variety of ways for that. One, from a technology perspective, state-of-the-art EMR that we can upgrade as well as from a growth perspective in terms of partnering with MPG and Apree. And then finally, and Gail mentioned this, but I'll reiterate it, a tremendous opportunity to wrap around existing Carelon Services to this arrangement that will create value for all 3 assets. So I appreciate the question.

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

And then one quick financial remark, just at the end of Pete's comments there, we do expect the consolidated entity once formed to have over $4 billion in annualized debt revenue.

Operator

Next, we'll go to the line of Dave Windley from Jefferies.

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

I'll switch topics over to Medicaid. Your redetermination enrollment impact seem to maybe pick up some momentum in the quarter. I think you said 90% of members have now been redetermined. I wondered if you could give us some view of kind of how you expect that to gate out over the next several quarters? And then from a risk pool and rate adequacy standpoint, could you update on how that looks now that the membership is whittling down?

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

I'm going to have Felicia Norwood address your questions.

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

Thank you for the question. Frankly, right now, we're at a point where our Medicaid business is actually tracking very much in line with our expectations. As you referenced, we believe that about 90% of our members have had their eligibility redetermined. So as we go through the next few months, you certainly see this tapering down as we really wrap up the unwinding process as we get through June. One of the things I want to make sure you understand, the downward trend in membership in the first quarter resulted not just from redeterminations, but footprint changes as well. So it's really the cumulative impact of those two things in terms of the first quarter. When we think about the work that we will continue to do is we will continue to outreach to Medicaid members.

Many members who have lost their membership at this point, did that as a result of really procedural reasons. So the team will continue to be very aggressive around continuing the outreach that's been going on, and we're really proud of the work that we continue to do to really reach out to over 4.5 million people, as Gail referenced in the opening comments, to make sure that individuals who are truly eligible for Medicaid have access to Medicaid and if not, are able to transition to an exchange product and continue coverage. In terms of where we are today with respect to the acuity and mix of that membership, the acuity is in line with what we expected.

And I will also say that at this point, we have visibility into 75% of our Medicaid rates and premiums for 2024. The vast majority of those are in line with our expectations and are actuarially sound. As you know, we have ongoing conversations with our state partners as we go throughout this process and we expect those rates to continue to be actuarially sound. So we're going to continue to work with our state partners. We're going to continue the efficacy with our members in terms of making sure they have access to care and coverage, and we're going to make sure that we go through this process with a lot of discipline and rigor, understand the mix of our membership and the leavers versus stayers as we go through this process.

Operator

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

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

I was wondering if maybe you could talk about utilization trends by line of business than what you saw in the quarter versus your expectation.

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

Lisa, thanks very much for the question. So utilization in the first quarter in our health benefits businesses was in line with our expectation, and that was reflected in our reported benefit expense ratio of approximately 85.6%. In the commercial business, specifically inpatient and outpatient authorization levels year-to-date were aligned with our expectations and our internal year-to-go trend remains unchanged. On Medicare, as expected, we saw utilization related to both the 2 midnight rule for inpatient stays as well as pockets of outpatient authorizations around, for example, radiology and cardiovascular procedures.

And importantly, these trends were broadly planned for as part of our underlying cost trend assumptions. Medicaid, as you heard Felicia talk about a moment ago, did experience increased but state-specific utilization attributed to the redetermination mix impact and we remain very comfortable with what we're seeing there, given those ongoing constructive dialogues with the impacted states. And so overall, we remain confident that both our MA bids for 2024 and our commercial pricing really reflect the appropriate projections for utilization and medical cost trends.

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. Just wondering if it's not a huge increase in guidance, but would love to kind of hear what was driving the increase in guidance? It's something -- is it on the health plan side? Is it on the Carelon side? And I guess just thoughts about how you thought about providing increases in guidance. It sounds like you believe that visibility is relatively high in claims, but obviously, there's some concern there. So I don't know if there's any conservatism or thought about pace of raises versus what you're actually seeing in the core business today?

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

We were pleased to report our adjusted diluted EPS this quarter, which came in slightly better than our seasonal expectation. And that was led by solid performance in both our health benefits and Carelon divisions, where operating margin increased by 30 basis points and 20 basis points, respectively, highlighting what we see as disciplined execution of our initiatives during a dynamic time for the industry. Of specific note, and you referenced this in your question, what is the favorable performance in the first quarter benefit expense ratio and that was driven by commercial margins that continue to recover from pandemic era lows.

We're very pleased with the Q1 results. It's still early in the year. And given our business is subject to some variability around medical cost trend, we're intentionally remaining thoughtful and prudent in our outlook and that led us to increase our guide for adjusted EPS by $0.10 to be greater than $37.20.

Operator

Next, we'll go to the line of Whit Mayo from Leerink Partners.

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

Just wanted to hear any comments on the external revenue growth with Carelon Services. Did that grow faster than the overall segment? You did, I think, referenced some strong external growth. So curious what might be gaining traction in the market. And then just a quick question on guidance. Mark, you've averaged maybe 55% to 56% of earnings in the first half. Any reason that would be different this year?

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

Great. Why don't I have Pete address sort of the Carelon questions, and then Mark will talk about the earnings percentages. Pete?

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

Yes, thanks for the question. As it relates to Carelon external growth, we continue to see really nice momentum in our build. I mean for 2024, from an overall sales perspective, we've already at this time of the year, exceeded what we did in all 2023. And you heard Gail mentioned in her prepared remarks, several new wins, which we're really excited about, really growth across the portfolio with some notable wins in behavioral health. She mentioned winning a statewide account in Medicaid for Maryland, which we're really excited about. And then some new innovative solutions with large employers as well as wins in the state of California.

And on the behavioral health side, also some select wins in the crisis space. So areas that we've been really focused on. In addition to that we've had some notable wins with the Blues related to our Insights business. We've talked about this before, but it's really critical that we prove some of our risk arrangements and our differentiated capabilities in Elevance and then port those to the Blues, and we've seen that play through with several notable wins. Lastly, I'd say we're excited about the '25 pipeline. We're obviously actively in the selling season. Our pipeline is very rich. And again, I would say a large focus on our insights businesses as well as our behavioral health businesses.

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

On your second question, the seasonality of the adjusted diluted EPS in 2024 is expected to be consistent with the past several years with approximately 55% of earnings in the first half of the year. I also want to call out that work days seasonality, given it is a leap year did result in a smaller than historically normal impact in the first quarter. But we expect the work days seasonality to put slightly more pressure on the third quarter MLR with an offsetting favorability than in the fourth quarter as those work days normalize.

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

Thanks, Mark, and thanks for the question, Whit. And I just want to add to Pete's comments about just the momentum that we're seeing inside of Carelon. First, our proof points are within Elevance Health. And then secondarily, now seeing some really nice momentum and traction externally.

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. Gail, I wanted to follow up on your comments on the Medicare business and the goal of balancing growth and margins. Could you maybe just elaborate on that given the tougher rate environment that you highlighted. And I think the company has prioritized margin improvement in Medicare this year, does that kind of remain on track for '24? And do you expect to plan for further improvement in 2025?

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

Thanks for the question, Nathan. As I shared in my opening comments, first of all, the Medicare rate announcement, as you've heard, represents second year of consecutive cuts to the program, that we know will result in increased premiums and reduced benefits for seniors with disabilities and particularly those that have really needed this program. Our approach is very consistent. We're going to continue to be disciplined in our approach to the Medicare business. Our focus is to get consistency high-value competitive benefits and balanced growth and margin. We're focused on building a sustainable, attractive long-term business. It's too early to provide specifics for the 2025 bid at this stage.

But again, I'm going to repeat, we're looking to really balance growth and margins. And as we talked about in our Investor Day, our focus is on keeping our members Blue for life. And there, we're focused on particularly our 14 Blue states and continuing to prioritize the very significant business we have in [GSNP] where our unique competitive advantage is serving the needs of those consumers with complex conditions. So overall, we're in the midst of the process right now. So we'll have more as we get through the bid process, but thank you very much for the question.

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*

Just interested, it seems like now you're talking about at least 12% EPS CAGR as your long-term expectations in both the slides and the prepared remarks. Like obviously, in the past, you've talked about a 12% to 15% EPS growth CAGR target. Just wondering what, if anything, we should be reading into that.

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

Thank you very much for the question. You should see these 2 targets as synergistic. We remain firmly committed to achieving a long-term adjusted earnings per share CAGR of 12% to 15% through 2027, as we communicated at our Investor Day event last year. And then as we think more broadly around the long term, we have confidence that through business cycles and over time, the earnings power of our health benefits in Carelon flywheel will generate the momentum and the foundation that's needed to sustain a long-term compound annual growth rate of at least 12%.

Operator

Next, we'll go to the line of Andrew Mok from Barclays.

Andrew Mok

Hoping you can give us an update on your transition of specialty scripts to BioPlus and help us understand the contribution that, that's expected to have this year.

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

Let me have Pete to address your question.

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

Yes. Thanks for the question, Andrew. Listen, the integration of BioPlus is going well. As you know, we remain on an accelerated calendar regarding this. I'll just reiterate, we spent last year building out the infrastructure and the team, and we did begin migrating scripts in January of this year. And we're doing so really on a stage basis. So we'll continue to do the migration throughout '24 and into 2025 as it relates to the Elevance Health book of business.

I'd say overall, things are going well. The infrastructure build is going well in addition to the BioPlus dispensing facilities that are in place. We're live with 1 additional facility now as we speak, and we have 2 more going live this year. So we feel very good about the capacity, not only with respect to the Elevance Health business beyond that. So we're excited we're on a path. And again, it will be staged throughout '24 and '25.

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

Yes. In addition, I'll just add to what Pete said to BioPlus. As you know, we also announced the acquisition of Kroger Specialty Pharmacy. And that is also well aligned to Carelon's effort to control those levers that matter. So Nick, thank you for the question.

Operator

Next, we'll go to the line of George Hill from Deutsche Bank.

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

First, I'd like to follow up on Dave's question on Medicaid. And I guess, can you talk about where you think we are in the kind of where in, I guess, in the calendar and the mix of rate determinations versus acuity mix and kind of -- I guess I'm trying to get a sense for how far behind do you think the kind of the rate repricings are versus the changes in acuity mix from redeterminations. And given that you just talked about specialty, I wonder if you could just add a comment on the Kroger deal and if you expect those scripts to transfer over to BioPlus and how you think about the stickiness of those scripts?

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

Yes, George, I think Felicia pretty much covered your question, which is, we think things are quite aligned at this point. So in terms of the acuity and the mix, everything, we have visibility into 75% of our Medicaid premiums. We've had very constructive discussions with our states. So overall, we feel things are lining up. They're actuarially sound, and our conversations are ongoing. So I feel very good about our Medicaid business, just to sort of put a finer point on that. In terms of Kroger, I'm going to ask Pete to comment on Kroger and how that's going to align with our broader pharmacy business.

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

Yes, George, thanks for the question on Kroger. And as Gail alluded to it, we're excited about this deal. It furthers the Carelon and the pharmacy strategy. It certainly is a natural extension of our recent arrangement with BioPlus. And just to give you some background, Kroger Specialty Pharmacy is the largest non-payer owned specialty pharmacy. They do about 500,000 scripts a year. And it really is a natural complement to what we're doing with both BioPlus and Paragon, quite frankly. To give you a sense of what this is going to do for us. It's going to add meaningful scale. It increases our access to more LDDs, limited distribution drugs, which is very important. Certainly strengthens our relationship with manufacturers, enabling us to really provide greater affordability and quality. And in fact, it has a nice presence in Puerto Rico, which could be very helpful to our MMM business.

As it relates to your question on transition of scripts, we feel very good about that. I mean, obviously, in this case, with specialty pharmacy providers and members have choice. But we feel very good about the execution model. We feel very good about the stickiness of the scripts, and we believe the integration and the transition will be straightforward. We expect the arrangement to likely close in Q3-Q4 of this year.

Operator

Next, we'll go to the line of Scott Fidel from Stephens.

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

Just interesting if we could double-click on the Carelon Services margins in the first quarter with the 90 basis points of expansion. Anything specifically that you would call out there and then that pacing does seem to be quite a bit stronger than the full year guidance where you had sort of called for flattish to down 30 basis points. So curious whether you have any updates for us just on how you expect Carelon Services margins to trend for the full year?

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

Thank you very much for the question. Margins were better than expected in the first quarter and that aligned very well to a very strong revenue growth in the quarter, given the launch of several new internal risk deals, which we expect to accelerate as the year goes on. We're not seeking to update our full year guidance at this time, given that both the seasonality of the business continues to evolve, as we expand our risk-based revenue and the timing of new product launches is anticipated to result in some transitory quarterly volatility. But let me turn it over to Pete for a couple of minutes to talk about what we're doing.

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

Yes. No, it's appreciated. And Mark's really covered it. But think about it this way. We are launching some pretty significant risk arrangements this year. We've talked about it, but a full risk arrangement in oncology, a full risk arrangement with the seriously mentally ill. And you should think about this as a natural cadence to launching this throughout the year and that's what's going to impact the margin. So for example, with the seriously mentally ill, we're doing this largely with the Medicaid business. It's not a big bang across all the Medicaid states immediately, as you'd expect. It's more methodical state by state in '24 and '25.

Operator

Next, we'll go to the line of Justin Lake from Wolfe Research.

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

There are some significant changes coming in the Part D space for 2025. I was curious as to your view on what that could mean for premiums. Just maybe you could tell us where you think kind of industry premiums are this year and how significant that increase could be for 2025?

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

I'm going to ask Felicia to address that.

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

So Justin, thank you for the question. There are significant changes coming for 2025. And I'll say this, it's early to provide specifics around what our 2025 strategy is going to be. But as Gail mentioned before, we are going to make sure that we have a very balanced approach as we think about the margins around our Medicare business and focus on those things that we believe bring the highest value to our members as we really work to make sure we have a competitive product in market that meets the needs of those members that we're trying to serve with a lot of dynamic changes that are going on in the Medicare environment for 2025. So thank you for the question.

Operator

Next, we'll go to the line of Ann Hynes from Mizuho.

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

Congrats on retaining the Florida contract, but it looks like you're actually gaining market share. Can you let us know the membership growth. And also looking ahead over the next couple of years, is there any big state renewal risk for Elevance, and alternatively, is there any big RFP opportunities for you?

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

We are certainly very pleased with the results in Florida. It's a state that we have been partnering in for a long period of time. But certainly, the win here allows us to expand our footprint and additionally serve some complex populations, particularly SMI, which will be very much kind of a collaboration with our Carelon Services business. So very excited about that. We are also very focused on our Virginia Go-live, which is coming up in July as well. So a lot of work happening there. Outstanding at this point is certainly Georgia, where we will be defending our procurement with respect to our core business as well as our foster care business in the State of Georgia and feel very good about the work that we continue to do there in partnership with the state.

In addition, we are very much focused on a couple of new geographies where we are bidding this year and look forward to hearing those results. But on top of that, the states are very much focused on specialty populations, and we see that as the opportunity for growth as we go forward. Medicaid is a very important business for us. Our recent RFP wins, I think, demonstrate the value that we bring to our state partners. But more importantly, the improvement in quality and outcomes that we are providing to Medicaid beneficiaries. So thank you very much for the question.

Operator

Next, we'll go to the line of Gary Taylor from TD Cowen.

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

Two quick ones for me. I just wanted to come back to Medicaid for a second. I mean, it's obvious your commercial book is doing very well, but you had expected Medicaid margins to come down this year, but you're saying the rate adjustments you're getting are actuarially sound for the acuity changes. So should we think about the lower Medicaid margins this year, primarily just the deleveraging, the OpEx impact of losing the revenue and enrollment and that MLR is going to be fairly stable? And then just my second question was, Mark made this comment. John made this comment for years about how days claims payable would eventually come down into the low 40s.

That's a lot of inherent or embedded earnings power that could come through the P&L at some point over time. Can you give us any sort of sense of what long-term means in terms of seeing the reserves move lower?

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

Let me start maybe with the margins, and let me bring it up to the health benefits business segment to talk about first. So in terms of health benefits, the margins this quarter were very much in line with our expectations. It puts us squarely on track to achieve our guidance for the full year of an increase between 25 and 50 basis points. Not looking necessarily to comment on a single businesses margin, but you could expect Medicaid margins to normalize given we already have line of sight, and you heard Felicia talk about this, into approximately 75% of the Medicaid premiums for 2024 and that we are comfortable with the actuarial soundness of the rates that we are seeing.

Over the long term, Medicaid continues to normalize, as we spoke about last quarter, and it is performing as expected. On DCP for 2024, if we look out through the end of the year, we anticipate remaining in the mid- to upper 40s range given Medicaid membership is expected to decline to within our guidance range of 8.8 million to 9.2 million members. And as you know, Medicaid has a slightly lower relative DCP compared to commercial, for example. And then over time to reiterate the guidance, we do expect over the long term DCPs to return to that more normalized range in the low 40s.

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

One more question, please.

Operator

And for our final question, we'll go to the line of Sarah James from Cantor Fitzgerald.

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

Just wanted to clarify a couple of things. One, on the reserve boost, are you saying that 1.7 days is fully related to conservatism via change because that seems like about a $600 reserve boost to us. So I wanted to see if there was any other factors in that 1.7 days. And second, could you give us a sense of your Medicaid rate seasonality? Like what percent of your book renews in 1Q versus 2Q versus 3Q?

Mark Bradley Kaye - *Elevance Health, Inc. - Executive VP & CFO*

On your first question, the sequential increase in days in claims payable a quarter result of 1.7 days is primarily related to the Change Healthcare. I just want to -- maybe one clarification around this. It's worth noting that neither the decrease in claims receipts that we saw during the quarter or the reserve accrual that we took related to Change Healthcare had any discernible impact on our benefit expense ratio or P&L and that's because we believe the reserve represents an amount you would otherwise have paid had there been no disruption. So you should think about this as overall for the quarter, incurred claims are completely consistent with our expectations. Given some of the notes that came out this morning, I also like to just reiterate that we do expect operating cash flow to be at least $8.1 billion for the full year, reiterating our earlier guidance.

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

And Sarah, just on your question with respect to our Medicaid states and when our rates are up for renewal, we have roughly 10 states that renew in January, another state that renews in April, another 9 that renew in July. And then the last 2 renew in the back half of the year in September and October.

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

Well, thank you very much for your questions. Just in some closing thoughts. We're very pleased to be off to a solid start this year, and we're confident, as you heard in the ongoing execution of our strategy and the balance and resilience of our diverse set of businesses positions us well for 2024 and beyond. We're very excited about the future and look forward to sharing more on our progress with you in the coming year. Thank you for your interest in Elevance Health, and have a great rest of your week.

Operator

Ladies and gentlemen, a recording of this conference will be available for replay after 11:00 a.m. today through May 17, 2024. You may access the replay system at any time by dialing (800) 876-4955. International participants can dial (203) 369-3997. This concludes our conference for today. Thank you for your participation and for using Verizon conferencing. You may now disconnect.