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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 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 Tanal - *Elevance Health Inc - Vice President - Investor Relations*

Good morning and welcome to Elevance Health third quarter 2024 earnings call. This is Stephen 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; Peter 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 and our revised outlook for the year and recent progress against our strategic initiatives. 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 Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you, Steve and good morning everyone. We appreciate you joining our earnings call. Today, we will review our third quarter financial results, discuss our outlook for 2024 and provide an update on the operating environment.

During the call, we will also highlight fundamental drivers of long term growth for Elevance Health which remains strong. For the third quarter adjusted diluted earnings per share were $8.37 which was below our expectations. Primarily due to elevated medical costs in our Medicaid business.

The impact on the third quarter and our full year outlook are being partially offset by focused medical management, the work we are doing with States to reflect the acuity of our members in rates, and proactive actions we are taking to enhance operating efficiency which will strengthen our business for the long term.

We are navigating a challenging and dynamic operating environment and have reduced our full year outlook to prudently reflect these challenges. Given third quarter results and our expectation that timing disconnects between Medicaid rates and acuity currently facing the industry will continue, we have reduced our outlook for adjusted diluted earnings per share to approximately $33. Importantly, we are not leveraging the future to achieve short term gains. We are investing to position Elevance Health for strong growth over the long term.

The issues impacting the Medicaid business are time bound and our state partners are working constructively with us on rate renewals. We're confident that rates will ultimately reflect the underlying acuity of our members, albeit on a lag, as States often use data that is more than a year old in setting rates. These short term headwinds are a byproduct of the large scale and unprecedented mix shifts associated with the end of the public health emergency.

Over the long term Medicaid managed care is an attractive business that is integral and complementary to our other health benefits and Carelon businesses and offers significant growth opportunities notably serving specialized populations where we provide distinct value with our unique capabilities.

Across our health benefits business, we are diligently executing on our growth strategy. Our Medicaid team is working tirelessly with our State partners and we appreciate the collaboration. While the rate increases we've received are the highest in the past decade, they're still inadequate to cover 2024 cost trends that we now expect to be 3 times to 5 times historical averages.

We're confident that rates will reflect the acuity of our members as enrollment continues to stabilize and we're acting with urgency to deliver significant operational efficiencies and appropriately manage the cost of care.

Partnering with States as they expand managed care to beneficiaries with chronic or complex conditions aligns well with our specialized whole health solutions, and is an important part of our growth strategy. In partnership with the Blue Cross Blue Shield of North Carolina, we're pleased to be expanding our service to North Carolinians through the recent award of a sole source foster care contract covering nearly 60,000 new members. This marks the second sole source foster care win in 2024.

In Medicare, we're taking deliberate steps to ensure the long term sustainability of our business. We are now two days into the 2025 annual election period and are pleased with our positioning overall. We remain disciplined in our approach to 2025 bids. Building on the actions we took to position our Medicare Advantage business for sustainable performance heading into 2024.

For 2025, we took a balanced approach to margin and membership, prioritizing the benefits seniors value most to mitigate the impact of CMS' rate cuts on beneficiaries and promote access to high quality, comprehensive and coordinated care for our members.

Given the benefit reductions and meaningful market exits we made heading into 2024, we maintained greater stability in our offerings for 2025, and as a result, we expect to grow individual Medicare advantage membership in line or slightly better than the broader market in 2025 led by products where we have strong sustainable market positions.

Medicare advantage star quality ratings remain a key enterprise priority, and we're committed to our long term goal of achieving and maintaining star ratings at the high end of all plans in our markets. For payment year 2026 we improved our own performance across nearly 60% of star measures and are pleased to be the only large payer to offer multiple five-star plans. Unfortunately, we will see the percentage of our members in plans rated four stars or higher decline due to significantly higher cut points.

The entire decline in our four-star member mix was due to one of our larger H-contracts narrowly missing a four star rating by four ten-thousands of a point. We have challenged our initial scoring with CMS and are considering all of our options.

Our commercial businesses are performing well and are on track to achieve their financial targets. We anticipate further growth in 2025 to be driven by increased penetration of our best-in-class products and services given momentum in both of our individual exchange and national account businesses.

For the largest employers, we offer differentiated value in innovative and attractive solutions. And our focus on whole health in partnership with Carelon is resonating. In our individual exchange business we're delivering particularly strong growth with membership up more than 30% year-to-date. As we look to 2025 we're expanding our individual and family ACA plans in three states, Florida, Maryland, and Texas under the Wellpoint brand, which will complement our existing presence in these states while driving growth for our health benefits and Carelon segments.

Focused geographic expansion enhances our ability to serve as a lifetime, trusted health partner to consumers in our communities.

Turning to Carelon, we're making significant progress in scaling our enterprise flywheel for growth. CarelonRx continues to expand its customer base while diversifying its value proposition. Earlier this month, we closed the acquisition of Kroger Specialty Pharmacy, which is aligned with our strategy of controlling the levers that matter and delivering whole health affordably.

Meanwhile, innovative solutions such as our SpecialtyRx Savings Navigator, Weight Management Solutions, and EnsureRx continue to gain traction and drive savings for our clients. Growth in Carelon services remain strong and we are on track to exceed the upper end of our initial outlook for low 20s percentage revenue growth. This includes external growth above our initial targets for 2024 - a proofpoint in first demonstrating our value proposition internally before driving growth externally. Carelon also recently entered into an agreement to acquire CareBridge, a value based manager of home and community based services for chronic and complex members that will serve as the foundation for Carelon's Home Health Business, and we're excited to continue to serve all its customers and members.

Carelon Services is expanding its capabilities to manage a growing proportion of health care spending supporting the long term growth of the business. And by extension, the value it creates for health plan customers.

Despite the challenges of the current environment, we're investing to position Elevance Health for sustained growth over the long term including through the application of AI Driven solutions that are enhancing member and provider experiences, reducing costs, and driving more efficient processes.

We expect to realize operational and financial benefits in 2024 and greater impact in 2025 and beyond. For our members, we're integrating AI across touch points to provide personalized digital service, improve access to care and further increase satisfaction.

We're also improving provider interactions and reducing costs by streamlining administrative tasks, automating onboarding, and enhancing contract administration. And for our associates, we're investing in tools that increase productivity, reduce manual tasks and enhance efficiency across the organization.

These are just a few of the AI applications we anticipate in the coming years. As we focus on programs that can have the greatest impact guided by a mission to provide unmatched value to our members, providers and associates.

In summary, our businesses remain fundamentally strong, and we remain confident in the flywheel for long term growth we're building with our complementary businesses. The issues impacting Medicaid are time bound and we're acting with urgency to improve performance and ensure adequate rates that reflect the acuity of our members.

We are confident that we're making the right investments to position Elevance Health for strong and sustainable growth over the long term in service of consumers across all age and income levels, and that we will emerge from this period of unprecedented change, stronger and even better positioned to serve the growing need for care management and cost containment in our health care system.

Before closing, I would also like to thank our dedicated associates for their tireless commitment to our mission and for the work they do each and every day to deliver for all of our stakeholders. It is their dedication and passion for those that we're privileged to serve that is reflected in our ongoing recognition as a great place to work for the fifth consecutive year.

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

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Thank you, Gail and good morning to everyone on the line.

As Gail shared, we reported third quarter results including GAAP diluted earnings per share of $4.36 and adjusted diluted earnings per share of $8.37 which came in below our expectations.

We ended the third quarter with 45.8 million members, flat sequentially. Growth in commercial was largely offset by the loss of approximately 85,000 Medicaid members due to a specific footprint change that took effect at the beginning of September. Year-over-year, commercial membership has grown by nearly 600,000, driven by strong fee based and individual ACA health plan growth on the distinct value we deliver to large employers and the targeted local positioning of our products.

Total operating revenue for the quarter was $44.7 billion, up over 5% year-over-year reflecting strong re acceleration in growth from the low point last quarter. The consolidated benefit expense ratio was 89.5% for the third quarter, an increase of 270 basis points year-over-year, principally due to Medicaid cost trend developing worse than expected. While Medicaid rate increases will reach record levels this year, they remain inadequate to cover cost trend that is in the range of 3 times to 5 times historical averages.

We are working closely with our state partners to ensure they fully capture the acuity of our Medicaid membership in future rates. During the quarter, we mitigated the impact through disciplined medical management and took further proactive actions to enhance operating efficiency across the enterprise.

As a result, Elevance Health adjusted operating expense ratio was 9.6%, an improvement of 150 basis points. Adjusted operating gain for the quarter was $2.4 billion and $8.3 billion for the year-to-date period, primarily reflecting declines in our Medicaid business.

We maintained a consistent and prudent posture with respect to reserves. Days in claims payable at the end of the third quarter, stood at 42.8 days which remains slightly above our targeted range in the low 40s. Given third quarter results and our expectation that cost trend in our Medicaid business will remain elevated through at least the fourth quarter, we have reduced our full year outlook for adjusted diluted earnings per share to approximately $33.

We now expect our 2024 benefit expense ratio will be more than 100 basis points higher than we anticipated last quarter, bringing the full year to approximately 88.5%. Full year operating cash flow is now expected to be approximately $4.5 billion.

It's important to keep in mind that the issues impacting the Medicaid managed care industry are time bound and we are confident that rates will ultimately reflect the underlying acuity of our Medicaid membership.

It's also notable that in 2024 businesses representing more than half of our revenues will be operating at margins below their long run potential. We expect margins will return to appropriate and sustainable levels over time.

Turning to 2025, we expect continued momentum in our commercial business bolstered by the expansion of our exchange offerings into three new states and the alignment of our value proposition in national and large group markets. We will deliver balanced growth in our Medicare advantage business and stability in Medicaid as redeterminations return to a normal cadence.

And we will further scale Carelon, our enterprise flywheel for growth with notable contributions from the expansion of specialty pharmacy dispensing capabilities in CarelonRx and continued momentum in Carelon services as we drive greater product adoption internally and externally and build out our home and community based business.

Finally, we are undertaking bold actions to modernize and transform many of our core processes through the application of new technologies that will create structural efficiencies and long term value. There is much to be excited about in 2025 and we expect strong acceleration in revenue growth at least in line with our long term growth algorithm in the high single digit percent range.

While we are confident that the issues impacting the Medicaid managed care industry are time bound, at this point in time, our outlook for 2025 adjusted EPS growth is at least in the mid-single digit percent range.

This reflects our assumption that the timing disconnect between Medicaid rates and acuity will continue. We will navigate this backdrop with the same focus and discipline that has been central to the long term success of Elevance Health.

Importantly, the earnings power of our diverse and complementary businesses remain strong and we are confident in our ability to deliver at least 12% growth in adjusted diluted earnings per share annually, on average, over time.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

AJ Rice, UBS.

AJ Rice - *UBS Investment Bank - Analyst*

Hi, everybody. Thanks for the question. So in the slide deck, you're reiterating your expectation of 12% earnings growth from '22 to '27, which off that '22 base would suggest you get something like $51 in '27. But you're also saying off the new base this year, you'll grow 5% next year, which would give you something like $34.65, something in a high $34s.

I guess the question is and it sounds like all of the short term issues are around Medicaid, is the getting the right rate going to be sufficient to get you the kind of accelerated earnings growth in '26 and '27 that would get you back on track to hit that multiyear 12% CAGR target or should we rebase that given what we're looking at 2024 and 2025?

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you for the question, AJ. Let me provide a little bit of high level perspective around that because I think there's, you have a lot of math in that question, but I think it's important, certainly appreciate the dynamic environment that we're currently operating in.

I think to really start that. First, we believe that the earnings power of our diverse and complementary businesses remains strong. So feel good about thinking about at least 12% over the long term and adjusted EPS over time. So I think that's important.

As you heard, and we're thinking about what's happening in our business right now. I'd like to sort of reiterate some of the things that Mark shared in his opening comments. First, strong acceleration in revenue growth, at least, in line with our long term algorithm in the high single digit percentage. So there's a lot I think to be excited about in our business momentum in our commercial business going strong.

We're entering several additional expanded ACA footprints next year, we feel good about the Medicare Advantage business, which we focus to be sustainable long term growth and Carelon is going to deliver even greater value as we look at the internal and external growth we're seeing in services and the robust pipeline in CarelonRx.

And then the last piece of that is continuing to realize substantial operational efficiencies. However, given, the dynamics that we spoke about in the environment that we're in, we anticipate that Medicaid margins in '25 are going to remain below our long term target. But again, this is a timing disconnect between rates and acuity, which we do believe is time bound, but think that can persist through 2025.

And also it's really important that we are going to continue to make ongoing investments in '25 because we think that there's a powerful opportunity across our business. So taken together, we think that we're being prudent in how we think about '25 and our expectations at this pace and timing. And that our guidance will give you a lot more detail in the fourth quarter. But I think you can rest assured we're going to continue to navigate '25 with the same focus and discipline that has been central to our long term success.

Next question. Thank you.

Operator

Stephen Baxter, Wells Fargo.

Stephen Baxter - *Wells Fargo Securities LLC - Analyst*

Hi, thanks for the question. Just wanted to come back to the Medicaid discussion. Obviously, the magnitude of the revision that's implied there is alarming, particularly given that we're at the end of the membership impacts from re-determinations, just trying to understand better how things got so much worse, so quickly.

I guess how much of this is actually new to the third quarter versus not having a good reading on where things were last quarter? And to the extent there are new developments in the third quarter, can you better help us understand? You know, perhaps what some of those are? Thank you.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. Let me ask Mark Kaye, our CFO to address your question. Thank you,

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Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Stephen, good morning. Let me start off by noting that we experienced accelerated cost trends in Medicaid throughout the third quarter. And additionally, we saw unfavorable prior period development related to the current year, specifically in our Medicaid business.

If I sit back for a moment, the Medicaid cost trends accelerated in the quarter. They restated negatively for the current year. And as such, we're tracking in the range of around --3 times to 5 times the historical average depending on the state. The elevated level of cost trend is driven, and you heard us address this in our prepared remarks, primarily by the higher overall membership acuity, given the redetermination cycle is now substantially complete.

And we are continuing to work with the States. We very much appreciate the collaboration. And while rate increases to date have also been higher than the historical average, they remain insufficient to fully cover the claims trends that we're seeing. And so it's important to keep in mind that the state processes themselves typically rely on reference periods that lag current experience by as much as one to two years. And while we are sharing more recent experience and trend information real time with the state, it's going to take time before that's fully reflected in their rate schedules.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. Next question, please.

Operator

Ben Hendrix, RBC Capital Markets.

Benjamin Hendrix - *RBC Capital Markets - Analyst*

Okay, thank you very much. Just wanted to kind of drill in a little bit more on the pacing of the catch up and of rates to acuity that you may expect over the coming year. You probably don't have perfect visibility into it. But are there any pockets, I think Mark mentioned a big bolus of members that kind of came off recently, it just are there any pockets of areas where you see a large bolus of members come off acuity increase and then have a state renegotiation that could be kind of a catalyst for creating some accelerated recovery or how do you think about pacing of the recovery throughout next year? Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks for the question, Ben, I'll ask Mark to comment on this as well. But I remember, you know, this is one of the largest and unprecedented mix shifts we've seen in Medicaid as the PHE has unwound over the course of the year. And again, as Mark said, what we saw was this acceleration through the third quarter. So I think putting that in perspective is really important. We have not had an environment like this before in Medicaid. So it's a very unusual time frame for us. But let me have Mark, give a little bit more color on that.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

I think the only thing I'll add to a Gail's remarks is that as we think about 2025, we do expect that mismatch between rates and acuity to narrow, especially as the state rate updates increasingly reflect the underlying member acuity.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. Next question, please.

Operator

Ann Hynes, Mizuho.

Ann Hynes - *Mizuho Securities USA LLC - Analyst*

Great. Thank you. Can you just give us a little bit more detail on the utilization trends? Like what is increasing more than your expectations? Is it inpatient outpatient pharmacy? Any color you could provide would be helpful. Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

I may have Mark address that please. Thanks.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Maybe let me take this briefly from two perspectives. I'll do a little bit of Medicare. Then I'll do a Medicaid. So Medicare in the quarter, you know was slightly elevated, it was manageable overall reflected some incremental pressure related to the two midnight rule. We also saw a late summer surge in COVID.

On Medicaid as I spoke about trends a minute ago, we are seeing some ongoing pockets of that elevated trend. They're most notable in the behavioral health area overall that we do expect margins to continue to remain pressured through the rest of the year. And certainly for those two businesses will remain below our long term average in 2025.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks. And again, our results were predominantly driven by Medicaid and as Mark said, we did see some slight pressure in Medicare but feel very comfortable about where we positioned our bids for 2025.

So, thank you. Next question, please.

Operator

Andrew Mok, Barclays.

Andrew Mok - *Barclays Capital, Inc. - Analyst*

Hi, this is Tiffany on for Andrew. It looks like the 200 basis points of 3Q Enterprise MLR miss like translates to about 500 basis points of Medicaid pressure in the quarter. One, is that the right ballpark to think about and two, like just given the apparent like hundreds of basis points of incremental pressure is the Medicaid book profitable today?

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. I'll ask Mark to respond to that as well.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Thank you very much for the question. The ballpark is about right for 2024. And as I think about the Medicaid business it is expected to be profitable this year. Albeit below our target margin range for the year itself.

And it's important to know that you really can't look at the Medicaid marginal business in any particular single quarter. You know, there are normal quarter-to-quarter dynamics of the business. But importantly, over the long term, we do expect the Medicaid Managed Care business to be a profitable and an attractive one for us and it's integral and it is complementary to other health benefits and Carelon businesses.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks for that mark. And again, just want to reiterate that, we do believe this is time bound. And we also believe that Medicaid is a very good business, particularly the specialized populations where we have unique capabilities.

But again, thank you for the question and next question please.

Operator

Erin Wright, Morgan Stanley.

Erin Wright - *Morgan Stanley & Co - Analyst*

And I wanted to ask on Medicare advantage, just based on the analysis of sort of the MA landscape now and the latest kind of benefit design details is there is the competitive environment playing out as you would expect in terms of being fairly rational with the focus on kind of profit versus growth? Is it playing out according to plan there? And in driving some of that assumption in terms of your at or above market growth in M&A next year. Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks for the question, Erin. You know, first, I think it's really important to realize we feel well positioned in MA. And we took a number of actions, prudent actions last year at the beginning of the year to position the business for long term.

Importantly, we had a number of market exits of markets we didn't think we saw long term sustainability. And this year, we continue to look for stability and make sure that we're in this business for the long term.

So I'm going to ask Felicia to comment now that we're a few days into AEP and give you a perspective of our thoughts on the market.

Felicia Norwood - *Elevance Health Inc - Executive Vice President, President - Government Business Division*

Thank you, Gail and, thank you Erin for the question. You know, our strategy as we look at Medicare Advantage really didn't start this year around our approach to balancing membership and margin. We started last year to really take strategic actions in order to create a sustainable foundation for growth in our Medicare Advantage business. And that included exiting several underperforming markets and that represented about 85,000 members.

In addition to that, we made significant reductions in our supplemental benefits in Puerto Rico on the heel of some losses in 2023. So if we put together our bid for 2025 we started the work with the foundation and wanted to make sure that we maintain stability where we needed to. But we wanted to be very focused on a balance between growth and margin, particularly in attractive and sustainable products and performance for us as we went forward.

Specifically, we focus very much on our D-SNP business in our high priority markets where we have the assets and the cost structure to really support leading market share. Additionally, I want to note that our products are predominantly HMO, not PPO and we were very prudent in our positioning, overlaying our local market dynamics and consumer preferences with our own market prioritization framework.

So when we look at where we are now, only two days into AEP, we feel very good about how we're positioned in terms of our key products and our target market. We prudently navigated the environment. And as we sit here today, as you said, we really expect to grow in line or slightly better than the market, but competitively feel we're very positioned well as we head into this AEP. Thank you.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. Next question, please.

Operator

Justin Lake, Wolfe Research.

Justin Lake - *Wolfe Research, LLC - Analyst*

Thanks. Good morning. I wanted to follow up on your comments around Medicaid trend accelerating through the quarter and being 3 times to 5 times typical to your point. I don't think anyone on this call has ever heard of trend being discussed in terms of multiples of typical. And given it got worse through the quarter, just curious if you could give us some color on what's going on through the quarter. Is it that you're seeing people come back on the rolls that are sicker, given the redeterminations themselves should have been, you know, give or take, run out at this point.

And then, you know, given that it looks like the exit rate in the quarter is the lowest margin, the highest cost sounds like. Can you tell us where you were ending the quarter and where you expect to be for the fourth quarter versus that 3% to 4% margin target that we all think about. Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks for the question. Just a couple of thoughts. And I'll ask Mark to provide a little bit more perspective. Remember again, this was the most significant change we've seen in membership in Medicaid probably as long as I've been in this business coming off of the PHE and again, the driver was this acceleration that we saw through the third quarter. And we did plan for accelerated acuity in our business, which I think is important.

But again, none of us when you're planning for 3 times to 5 times the cost structure, we've been working very diligently with our state partners in terms of understanding those rates and where we need to be. And again, they are looking at data often times a year in arrears and have been responsive to changing their process. But it has not kept pace yet and we think it will take them some time.

With that, let me ask Mark to give a little bit more perspective on some of the other questions that you had embedded.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Just to add additional color here, as you heard from Gail. We definitely planned for an elevated level of trend in 2024 relative to the historic average Medicaid trend, which has run in the low single digit percent range. And to the point we made earlier, that trend is now running around 3 to 5 times historic average levels of course, depending on the states and meaningfully above our expectations.

And that's really driven by this unprecedented redetermination related activity, which has resulted in several downstream changes in membership mix, membership count, Acuity program adjustments, et cetera. I'd also like just to reiterate sort of that long term target for Medicaid is in that 2% to 4% range.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

And finally, just to your point, we've also not been standing still. Obviously, we've been very active in managing the things that we can control around cost structure and acceleration of initiatives that we had in place around AI and making our business sustainable for the long term.

And again, very active with our state partners, proud of our teams for the work that they've done to bring this forward. But again, we do think this will take time to work with our state partners to get the match at the appropriate level.

So thanks for the question and next question, please.

Operator

Lisa Gill, JPMorgan.

Lisa Gill - *JPMorgan Chase & Co - Analyst*

Thanks very much and good morning. Gail, one of your peers talked about accelerating Rx trends, and specialty. You know, we've seen changes to IRA around catastrophic coverage, the one you haven't called out anything around Rx as far as cost trend goes. Are you seeing that? How did you price for that going into 2025? And then just on the flip side, CarelonRx had very strong results, is that a key driver of what we're seeing, especially on the specialty side and growth in specialty.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

So, thanks for the question, Lisa. Let me get a little perspective directly on your question and I'll ask Pete Haytaian, who leads our pharmacy business to provide some more contacts. So year-to-date, we have seen an increase in Medicare advantage part D specialty drug utilization. But the trends in unit cost have been in line with our assumptions. So we don't see it as a significant impact to what we've been talking about.

Let me ask Pete to give you a little more perspective on what's happening in terms of overall pharmacy.

Peter Haytaian - *Elevance Health Inc - Executive Vice President and President, Carelon and CarelonRx*

Yeah. Thanks Lisa for the question. As you said, we were very pleased with what we're seeing, you know, in terms of our CarelonRx strategy and growth. We continue down our path of insourcing the strategic levers that matter, down our path of specialty pharmacy and infusion. We're making really good progress there.

And as it relates to growth, our story is resonating in the marketplace. We're beginning to see a lot of pull through in that regard and we've had some nice wins going into 2025 upmarket as well. So that is all proceeding as planned.

In terms of our overall, performance from an operating margin perspective though, as Gail said, we did expect what we saw in the specialty pharmacy trends, we did see that increase, but it was really as expected when you look at our overall margins, the out performance in the quarter was largely due to a one time favorable revenue adjustment that was intra year. And when you, even that out or spread that out through the year the full year still remains on track in terms of our initial guidance around the 6% - 6.5% margin profile. So we feel overall very good about where we are and where we expected to be.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks Pete. Next question, please.

Operator

Lance Wilkes, Bernstein.

Lance Wilkes - *Bernstein & Co. LLC - Analyst*

Quick follow up on the rate outlook for Medicaid, if you could just give some color on what you observed as far as rate increases, maybe historically or in the first half of the year and then what you're seeing in the second half of the year and what your outlook is based on how far you are along in early '25.

And then the broader question was just, are you, are you anticipating making any strategic moves as a result of these pressures that again are time bounded? And as part of that, does this make any change in how you might insource all of the functions of your PBM? Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

So a lot of questions here, Lance. Thank you. Let me, let me just address your question on strategic. Then I'll ask Felicia specifically talk about Medicaid. You know, we feel we've laid out a very comprehensive strategy around the growth drivers and the opportunities as I shared in the first question, really, how we see acceleration in revenue and strong commercial business. We believe that time bound issues around Medicaid. And we think we will work through those with the assets we have.

And then Medicare being well positioned and Carelon is a real accelerator for us. And as you saw, we announced an additional acquisition this morning as part of CareBridge that gives us home based care and another pillar inside of our growth strategy for Carelon services where we can take significantly more pass through of the type of medical expense we're managing inside of Carelon.

So I would say, we're very focused on the long term growth drivers and our flywheel for growth inside of Elevance Health and feel very positive about the fundamentals of our business. So strategically, I think we're moving forward in the exact same path that we've laid out and in the pharmacy side taking more control of the levers that matter for us.

And you've continued to see us integrate the Kroger specialty pharmacy acquisition, our advanced home delivery. So feel very good about that progress and we're dealing with the time based issues in Medicaid right now. But let me ask Felicia to address the Medicaid specifically.

Felicia Norwood - *Elevance Health Inc - Executive Vice President, President - Government Business Division*

Good morning and thanks for the question. You know, if you can imagine the rate negotiations with our state partners are ongoing. And when you take a look at how our portfolio of business is spread out across the year, we have about half of our states that are January States and the other half that are July States and in the back half of the year, the work that we started with our state, certainly around the July States and rates certainly took a look at the '25 rates that they were working with us on.

But we also put a lot of work to work with our states on understanding the trends that we're seeing in the first half of the year. As you heard earlier, the reference period for most of our states are 2023 when you think about the '25 rate setting process. So there will certainly be that misalignment and that timing mismatches, we talk about.

When we look at the work that we're seeing with our state partners. Some states have certainly been more receptive to going back and taking a look at those and addressing those rates now. We've had certain states that have given us mid-year rate adjustments and more of those will happen as we go through the back half of the year and early next year as well.

But as you heard earlier, this is a process which you clearly understand that will take some time to actually get total alignment between our rates and the acuity of the membership that we're seeing on the heels of an unprecedented change and mix with respect to this business.

But I will tell you, we are going to continue our strong advocacy working with our state partners, sharing up to date information around the changes that we're seeing and we have full confidence that we will ultimately have rates that are aligned with the acuity of the membership in our population. So thank you for the question.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. Next question, please.

Operator

Joshua Raskin, Nephron.

Joshua Raskin - *Nephron Research LLC - Analyst*

Hi, thanks sorry to stay on the topic, but I'm still struggling with why the acuity rate mismatch is accelerating now or why this cost trend is accelerating now. My understanding is that most of the redeterminations, you know, have been done, right? This started over a year ago. So felt like there was less redetermination activity in the most recent quarter than previously.

And I think, last quarter, there was this conversation around higher utilization for members that were about to lose coverage. And so you would have expected that to slow. So I guess I'm still confused as to what's causing this big acceleration in this trend. Why is that happening so late in the process?

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Josh, good morning and thanks very much for the question. Two key points. I'd like you to keep in mind here.

First, we've modeled a prudent view of costs for the fourth quarter and you could think about that as us holding Medicaid trend, approximately flat relative to where we were in September.

And the second key point to keep in mind here is that we had unfavorable development related to the current year in the quarter.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Next question, please.

Operator

Michael Halloran, Baird.

Michael Halloran - *Robert W. Baird & Co., Inc. - Analyst*

So, just to add on the Medicaid topic. So based on your '24 guide, if I'm not mistaken, implied, 4Q impact actually seems to be larger than your third quarter MLR Pressure. So it sounds like this is the case. But is this basically assuming the acuity rate mismatch worsens in the next quarter even though you have all your September/October rate increases.

And at this point, I guess in mid-October, do you think you now have enough data and visibility into your own acuity mix that you can pass along to these states in time for Jan one renewals or just, you know, I presume draft rates are pretty already there. So could they open that back up and adjust or is it too late? Thank you

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Yeah, a couple of things, just high level one, you also have to factor in a seasonality into the fourth quarter. So make sure you're doing that and I'll ask Felicia to talk a bit about Medicaid and the process that just goes on a rate setting.

Felicia Norwood - *Elevance Health Inc - Executive Vice President, President - Government Business Division*

Yeah. So, you know, thank you so much for the question again. You know, at this point, we have about 55% of our rate visibility for premium for January. However, those are draft rates. So we spend a lot of time with our states right now making sure that they understand the experience that we were seeing in the second and third quarters as we head into the rate setting process.

So yes, when we have draft rates, the process is still iterative and ongoing and we are continuing to make sure that the states have visibility around that information. So we have 55% as I said, of visibility into the January renewals, but those are early discussions, Michael and expect a lot of work to happen between now and the end of the year in terms of the work between us and our state partners.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Maybe one to comment just to add on to Felicia's remarks. Just to reaffirm, Medicaid trend is not expected to accelerate in the fourth quarter. It's primarily seasonality that's resulting in these numbers.

Next question, please.

Operator

Ryan Langston, Cowen.

Ryan Langston - *TD Cowen - Analyst*

Hi, good morning. It sounds like you expect growth on the exchange side into 2025. So I guess in that context, how should we think about the margin profile for maybe just the exchanges in the overall commercial business? I think you can --

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Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you very much for the question. We'll have Morgan Kendrick, who leads our commercial business respond to that.

Morgan Kendrick - *Elevance Health Inc - Executive Vice President, Elevance Health and President, Commercial and Specialty Health Benefits*

Ryan, thank you for the question. We act, we feel really good about our commercial business in aggregate and certainly the individual ACA is a big piece of that. We've taken a very disciplined approach over the last 36 months in gradually expanding our footprint and our competitiveness in our 14 geographies, as Gail mentioned in the prepared remarks up front, we're expanding that in other markets.

So this year, we're expecting to have nice growth in our markets, probably improving share in the markets that we served by about two points moving forward. That said when I think about next year, we're positioned really well and in the geographies where we've already served, We're in the process of sort of determining the positioning in the markets that we're moving into, but are really excited about that business. And it also being in line with our expectations on the economics.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. And, just another thing to remember, those are states where we also have Medicaid and Medicare business. So it aligns with us knowing those states well.

Thank you. Next question.

Operator

Scott Fidel, Stephens.

Scott Fidel - *Stephens Inc. - Analyst*

Hi. Thanks. Just interested if you could maybe dimension for us and discuss some of the downstream impacts from the Medicaid environment to the Carelon health businesses. Do know that there's quite a bit of leverage or exposure in those businesses to Medicaid. So curious , on how those businesses are performing and how you're positioning them around some of these dynamics we're seeing a Medicaid. Thanks.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Yeah, thanks for the question, Scott. I'll ask Pete to address your questions.

Peter Haytaian - *Elevance Health Inc - Executive Vice President and President, Carelon and CarelonRx*

I think it's a great question. I appreciate it. First, just stepping back and thinking about Carelon overall and as you heard in the prepared remarks. Overall, very pleased with the growth trajectory of Carelon Services exceeding 30% growth in the quarter, a quarter year-over-year, not on a path to exceed initial guidance of the high teens low '20. So we feel very good about that.

And as it relates to growing internally and externally, I'll say that we're, we're continuing down the path that we've been in with regard to proving out our solutions internally and then growing externally, I did want to point out that and as Gail mentioned in the prepared remarks, seeing really nice traction externally, I'd say 4 times improvement in terms of growth in 2024 and good visibility on 2025.

As it relates to your question. Specifically, yes, we do have products oriented to Medicaid, Medicare, we are taking full risk and as it relates to our performance overall, we are seeing some of those behavioral health trends play through. So when you look at the margin profile in the short term, we are being impacted by the behavioral health trends, we are also being impacted by the acceleration some of the risk arrangements that we're deploying.

And as you recall, I think I've said it in the past early on when we launch these risk arrangements, the margin profile is a bit more compressed and then as it evolves, it improves. So the combination of those two factors is what's been affecting us in the short term. We feel very good about the long term and continuing to grow within the government program business as well as in the commercial business. We are pursuing a diversified approach just like the rest of Elevance Health.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Next question, please.

Operator

Whitman Mayo, Leerink Partners.

Whitman Mayo - *Leerink Partners LLC - Analyst*

Hey. Thanks. I just wanted to go back and follow up. I think it was Justin's question, not sure I actually heard the answer.

Are the rejoiners coming back negatively impacting cost trend, like are they increasingly gaining access through the point of care through presumptive eligibility in the hospital or something like what does the actual care activity look like on the joiner population?

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

It's Mark here. Thank you very much for the follow-up here. There are a number of trend factors that are remaining to various degrees. And certainly, some have improved over the past quarters, think about like the pull forward effect to think about member mischaracterization and certainly some that are ongoing.

Really important here is that the state actuarial rate process and our ongoing discussions with them really aim to capture the overall cost of the members in ensuring the adequacy of rates over time. On your question specifically, you could think about a portion of trend is being attributed primarily to the acuity mix shift versus, I think we spoke about last quarter, so that same-store type trend or utilization.

And you could think about approximately 60% of the trend as being related to acuity mix. And the key point, as I'm going to sort of end here is that our embedded Medicaid outlook really does include prudent assumptions for cost trend in the fourth quarter, inclusive of all the underlying factors.

Operator

Sarah James, Cantor Fitzgerald

Sarah James - *Cantor Fitzgerald & Co. - Analyst*

Thank you. Mark, when you said Medicaid is profitable in '24, is that across all states? Or is it a mix of some profitable and some not. And then can you just help us understand the actuarial soundness protection? Is that a two-year or a three-year period? If we look at '24 and '25 as below target margins. But I think '23 was a good year for you guys on Medicaid. Does that still give you a position to pursue retroactive rate increases on top of the midyear rate updates you're targeting?

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Sarah, thank you very much for the question here. I'm not going to talk about states specifically. But simply just to note, Medicaid margins on the whole are expected to compress significantly this year. And we started out this extensively.

This is the industrywide timing disconnect between rates and acuity. Our long-term expectations are unchanged. And that's because we are continuing to proactively collaborate with our state partners on integrating acuity into the rates that we're seeing. We know that's going to take time based on the state processes, the collection of data etc.

And so, we're very confident that over time, rates will certainly appropriately on an actuarial and otherwise basis reflect the underlying acuity that we're experiencing. And so, I would certainly say that we are confident in our long-term targets that we have set out and we're committed to achieving them.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thank you. And just reiterating, I think we do believe Medicaid is a long-term very good business for us. It's complementary to our other health benefits business and particularly around other specific populations that we think we have very unique skills to serve those. So again, thank you very much for your questions. We see Medicaid as a long term and this being an industry, time-bound issue.

Next question please.

Operator

Dave Windle, Jefferies.

David Windley - *Jefferies LLC - Analyst*

Hi. Good morning. Thank you for taking my questions. I wanted to try to understand, respectively, the comments about kind of the cadence of rate recovery or achievement in Medicaid and then the confidence in MA bids for Medicare and with the question being in your mid-single-digit EPS growth for next year, do you expect margins in caid and care, respectively, to be up, flat or down?

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

So thank you very much for the question. Let me ask Mark, first to address your questions on margins. And then, obviously, at this pace, we'll give you some directional commentary because it's still early in the year for '25 but we'll give you at least a sense of how we're thinking, Mark.

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Overall, we expect for 2025 margins to continue to remain strong in commercial. Let me start there. On the Medicaid side, here, margins will remain below our long-term margin range and that's really predominantly related to the timing match that we've spoken about. You could think about them as effectively being stable year-over-year.

And then, on Medicare, because of the sustainability around our 2025 product positioning, we actually expect margins to improve in 2025 compared to 2024.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Thanks for the question. Next question, please.

Operator

Joanna Gajuk, Bank of America.

Joanna Gajuk - *BofA Securities, Inc - Analyst*

Hi. Good morning. Thanks so much for taking the question. So just last question, I guess, on this Medicaid commentary, and I guess the margin commentary you just made in terms of margins being stable to be in next year. Is that I guess, confirmation that you assume that by the end of '25, the Medicaid rate mismatch will be fully restored? Is that the way to read by the end of the year, it's going to be restored?

Mark Kaye - *Elevance Health Inc - Chief Financial Officer, Executive Vice President*

Thanks for the question. Let me actually step back for a second and think about MLR guidance for 2025, and we're not looking to provide that necessarily today, but let me share a few modeling considerations that might help you. First, again, with respect to the third quarter, we had some out-of-period items, including unfavorable intra development for the Medicaid business, and we do not expect that to repeat.

As we progress toward and through 2025, you could think about that as a first half, second half story, where we expect the rate versus acuity mismatching Medicaid to narrow as the year progresses and as rates continue to improve.

It's also important when you think about the modeling for the business to remember that January 1 is a major renewal base in our commercial business, right. And that marks the beginning of an end, we also marked the beginning of a new plan year for Medicare. So we're remaining intensely focused on the appropriate medical management, and that's going to continue through 2025. I would say otherwise, it's too early to provide specific individual line of business guidance as we head into next year.

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

Right. And thanks, Mark. And just to reiterate that, we're taking a prudent view of the timing on the mismatch in Medicaid and want to be respectful of the state process and the work we're doing, we feel that it has been a very good process with the states. But again, they have to get their data from prior periods.

And so, we're trying to update them on what we're seeing. So again, it's early in the timing, but we wanted to give some sense of our confidence in the long term of our business and the fundamentals. But again, I want to take a prudent view of what's happening in Medicaid, particularly on the state rate. We'll have one more question, please.

Operator

George Hill, Deutsche Bank.

George Hill - *Deutsche Bank AG - Analyst*

Hey. Good morning, guys. And just kind of a couple of quick follow-ups here on the Medicaid again. I guess number one, -- , could you provide more color on what drove the PYD in the quarter? And then, I guess from a state concentration perspective is kind of -- is the discrepancy between rates and acuity broad-based? Or is -- are there state concentrations here that we should be concerned about, like that could speed the resolution of the issue?

Gail Boudreaux - *Elevance Health Inc - President, Chief Executive Officer, Director*

So in terms of your overall question, clearly, we manage a portfolio of states, and we don't get into specific states. But every state is a little bit different based on the population we serve and the programs that are in place. So I wouldn't make it generalized across all states. I know that we are working very diligently with each of the states to make sure -- and again, this is industrywide, not just unique to Elevance Health, and we see this across everything.

So thank you very much for the question. And now we'll turn, I think, to, first of all, say thank you, operator, and thank you for all the interest and support of everyone who has been on the line. I just want to reiterate, we're confident that we're making the right investments to position Elevance Health for strong and sustainable growth over the long term and that we are confident we're going to emerge from this period of unprecedented change even stronger. Thank you, everyone, for your interest in Elevance Health, and thank you for joining us on this call.

Operator

Ladies and gentlemen, a recording of this conference will be available for replay after 11:00 AM today through November 16, 2024. You may access the replay system at any time by dialing (866) 510-4837, and international participants can dial (203) 369-1943.

This concludes our conference for today. Thank you for your participation and for using Verizon conferencing. You may now disconnect.