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CI.N - Q4 2020 Cigna Corp Earnings Call

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OVERVIEW:

Co. reported 2020 consolidated adjusted revenue of $160b, consolidated adjusted after-tax earnings of $6.8b and consolidated adjusted EPS of $18.45. Expects 2021 consolidated adjusted revenues to be at least $165b and consolidated adjusted income from operations to be at least $6.95b or at least $20 per share.

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PRESENTATION

Operator

Good morning. Ladies and gentlemen, thank you for standing by for Cigna's Fourth Quarter 2020 Results Review. (Operator Instructions) As a reminder, ladies and gentlemen, this conference, including the Q&A session, is being recorded.

We'll begin by turning the conference over to Ms. Alexis Jones. Please go ahead, Ms. Jones.

Alexis Jones - *Cigna Corporation - IR Lead Principal*

Good morning, everyone, and thank you for joining today's call. I am Alexis Jones, Lead Principal for Investor Relations. With me on the line this morning are David Cordani, our President and Chief Executive Officer; and Brian Evanko, Cigna's Chief Financial Officer. In our remarks today, David and Brian will cover a number of topics, including Cigna's full year 2020 financial results as well as an update on our financial outlook for 2021. As noted in our earnings release, when describing our financial results, Cigna uses certain financial measures, adjusted income from operations and adjusted revenues, which are not determined in accordance with accounting principles generally accepted in the United States, otherwise known as GAAP.

A reconciliation of these measures to the most directly comparable GAAP measures, shareholders net income and total revenues, respectively, is contained in today's earnings release, which is posted in the Investor Relations section of cigna.com. We use the term labeled adjusted income from operations and adjusted earnings per share on the same basis as our principal measures of financial performance.

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In our remarks today, we will be making some forward-looking statements, including statements regarding our outlook for 2021 and future performance. These statements are subject to risks and uncertainties that could cause actual results to differ materially from our current expectations. A description of these risks and uncertainties is contained in the cautionary note to today's earnings release and in our most recent reports filed with the SEC.

Before turning the call over to David, I will cover a few items pertaining to our financial results and disclosures. Regarding our results. In the fourth quarter, we recorded an after-tax special item benefit of $3.2 billion or $8.91 per share for the sale of Cigna's Group Disability and Life business that was completed on December 31, 2020.

We also recorded an after-tax special item charge of $148 million or $0.41 per share for integration and transaction-related costs. As described in today's earnings release, special items are excluded from adjusted income from operations and adjusted revenues in our discussion of financial results.

Beginning next quarter in our earnings release and quarterly financial supplement, the Group Disability and Other segment will be combined with Corporate and called Corporate and Other Operations. This change to simplify our reporting was enabled by the aforementioned sale of the Group Disability and Life business.

Additionally, please note that when we make prospective comments regarding financial performance, including our full year 2021 outlook, we will do so on a basis that includes the potential impact of future share repurchases and anticipated 2021 dividend.

With that, I will turn the call over to David.

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Thank you, Alexis. Good morning, everyone, and thank you for joining us on our call today. When we met a year ago, the challenges from COVID-19 were just beginning to fully emerge around the globe. With the arrival of vaccines, 2021 is likely to be a year of transition as communities and businesses seek to turn the page. I am very proud of the ways in which our 70,000-plus colleagues led and continue to lead through this difficult time for customers, our clients, our providers, our partners and our communities.

Starting last spring, we were amongst the first to wave out-of-pocket cost for COVID-19 testing as well as treatment. Our Evernorth business quickly leveraged our supply chain expertise to ensure consistent prescription drug supply and delivery during the uncertain times.

In our U.S. Medical business, we ramped up to meet the significant increased demand for behavioral health services by growing our network, adding virtual provider partners, creating on-demand webcasts, treating first responders and adding search capabilities for provider ethnicity. All while we were deploying hundreds of millions of dollars to support our clients and partners who are hit hardest by the pandemic.

In partnership with New York Life, we launched the Brave of Heart Fund to provide charitable grants for families, frontline workers and volunteers who lost loved ones to COVID-19. Then last month, our Cigna Medical Group was amongst the first non-hospital organizations in the nation to administer antibody therapy for high-risk COVID-19 patients, freeing up much needed hospital space. And just a few weeks ago, we partnered with industry leaders from across the public and private sectors to ensure that people who receive the vaccine have digital access to their vaccination records so they can safely return to their jobs and daily activities.

As we continue to work to serve our clients, our customers and our patients during the pandemic, we also balanced our responsibility to deliver for our shareholders as well. For 2020 full year, we grew our adjusted revenue by 14% to $160 billion. We also delivered adjusted earnings per share of $18.45, consistent with our overall expectations, which included the ongoing elevated cost of COVID-19 related services.

Today, I'm going to talk about how our strategic actions we took in 2020 position each of our businesses to navigate what we expect will be another very dynamic year, one that will require us, again, to balance the varying needs of all of our stakeholders. I'll also tell you about our growth framework

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and how our execution of it will drive our success throughout this challenging environment and beyond. Following my comments, Brian Evanko will share more details about our 2020 financial results and our 2021 outlook. And then we'll take your questions.

At Cigna, we've been on a journey, an important one over the past 2 years to significantly accelerate our strategic path. During 2020, we completed the integration of our combination with Express Scripts and delivered on our integration priorities, including revenue growth, cash flow generation, deleveraging targets, strong client retention, high levels of coworker retention and working to keep our vision top of mind with innovations and improved affordability, predictability and simplicity delivered to the market.

In addition, we delivered another important milestone of our strategic journey by launching Evernorth, our health services platform, which has meaningfully grown our strategic partnerships and is bringing innovative solutions to the market already. We also recently made a series of leadership changes to align our capabilities and further operationalize our strategy reinforcing our talent depth and our commitment to continue to grow and develop our team. And based on the capital and cash flow strength of our company, we are demonstrating the ability to have an "and" orientation to our capital deployment strategy. This means we're able to reinvest in our business for ongoing growth, and pay a meaningful quarterly dividend, and deploy substantial capital to share repurchase, and target and pursue strategic M&A.

At the same time, we continue to execute effectively across each of our businesses by delivering value to our clients and customers or patients. In Evernorth, our 2020 adjusted revenue increased 20% driven by ongoing strong retention, the completion of insourcing Cigna volumes and organic growth, including our partnership with Prime Therapeutics.

In U.S. Commercial, our relentless support of our customers and our employer clients and partners throughout the pandemic led to strong client retention levels again in 2020, along with better-than-expected in-group strength building a solid foundation that we will carry into 2021.

In U.S. Government, we grew our Medicare Advantage customer base by 18%, exceeding our average annual growth target of 10% to 15%, and we expanded our geographic and product footprint to now be making market offerings in 28% of all available Medicare Advantage buyer markets.

In addition, 88% of Medicare Advantage and prescription drug plan customers in 2021 are in 4-Star plus rated plans, with our national weighted average of 4.5 Stars, the highest amongst our national competitors. And in our International business, despite navigating the challenges of the ongoing pandemic in multiple countries, we delivered full year adjusted earnings growth of 18%, fueled by our strong partnerships.

Related to the Group Disability and Life, which we sold to New York Life on December 31, I am proud of the way in which our team worked to deliver in a very challenging environment, fueled by the pandemic for the benefit of our clients and customers. As a result of the pandemic, it created a significant reduction in our earnings contribution for our business last year. However, we remained focused on serving our clients and customers.

Throughout 2021, we expect the macro environment to remain dynamic, which presents both challenges and opportunities for us. Among the challenges, we expect COVID-19 and the rollout of the vaccine to continue to tax an already overburdened health care system. And we expect intensified and much-needed focus on health disparities to continue as well. At the same time, we also see opportunities. They include greater recognition of the importance of the employer-sponsored market, with companies playing an even more critical role in ensuring the well-being of their employees by offering comprehensive medical, pharmacy and behavioral services.

There are also a number of accelerating trends that will further drive fundamental changes in health care. For example, pharmacological innovations are quickly becoming the future of health care, driven in part by the continued rise in specialty pharmaceuticals, gene therapies and the evolution of biosimilars. There's also greater recognition and acceptance of the link between mental health and physical health. And we see care access rapidly changing as a result of consumer behavior and technology and data innovation, leading to growing use of virtual visits and coordinated home-based care, all aided by advancements in remote monitoring as well.

Against this backdrop, the progress we achieved in 2020, along with the strength of our capabilities, that gives us confidence that we will deliver at least $20 of adjusted earnings per share in 2021, even in the face of the COVID-19 headwinds, primarily in the form of elevated medical costs.

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Our ability to achieve this level of continued long-term success starts with our growth framework, which is 3 fundamental building blocks: First, we delivered differentiated value in the form of affordable, predictable, simple solutions for our clients, customers and patients. This drives our ability to retain, further deepen and grow our business platforms. Second, we work to partner and innovate. This enables us to rapidly bring new solutions to the market that create even more value for our clients and customers. And it also fuels our third priority, the expansion of our addressable markets, which we'll achieve by growing our geographic footprint further by moving into underpenetrated markets through service coordination and through addition of new solutions that gives us the opportunity to sell to new buyer groups.

Taken together, these building blocks provide us with multiple levers to continue to achieve differentiated and sustained growth, not only in 2021, but over the long term.

In Evernorth, this means bringing an expanded set of solutions to our existing health plan, Commercial and Government clients by leveraging the strength of our pharmacy, care management, health intelligence and benefit management capabilities.

In U.S. Health Care, this means continued outstanding retention, along with further deepening relationships and target new business adds. In U.S. Government, it means delivering on our goal of accelerated customer growth of 10% to 15% in Medicare Advantage. It also means continuing to expand our geographic footprint in the individual exchange market, where, for example, in 2021, we'll be offered in 220 counties. This is a more than 50% year-over-year increase. And in International, it means continuing to grow as we deliver differentiated value for our globally mobile customers as well as our supplemental health solution customer. We look forward to delving more deeply into our growth strategy with you at our Investor Day, which is slated for March 8.

So now to summarize, I am very proud of our colleagues and our company for delivering for our customers, patients, clients, partners and shareholders in an extraordinary year by maintaining a relentless focus on delivering on our commitments and leading through a rapidly changing landscape. Our performance is a testament to the resilience of our organization and our ability to thrive and deliver differentiated results in the most challenging of environments. We delivered strong revenue, earnings and cash flow results in 2020.

In 2021, we expect to deliver at least $20 of adjusted earnings per share, and we will continue to drive attractive operating cash flow, which fuels our ability to return value to our shareholders through a meaningful quarterly dividend and through ongoing share repurchase as well as targeted M&A. Overall, we have confidence that we will achieve our 2021 outlook and our long-term growth objectives.

With that, I'll turn the call over to Brian.

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Thanks, David. Good morning, everyone. First, as we look back at 2020, I'm very proud of the actions we've taken as a company to meet the needs of our customers, clients, provider partners, communities and co-workers while also delivering on our commitments to our shareholders. And as we enter 2021, we remain focused on delivering differentiated value and driving growth across our businesses.

In my remarks today, I'll review Cigna's 2020 results, including the ongoing impacts of COVID-19 on our business and provide our outlook for 2021.

Key consolidated financial highlights for 2020 include adjusted revenue of $160 billion, adjusted earnings of $6.8 billion after tax, adjusted earnings per share of $18.45 and operating cash flows of $10.4 billion. These results reflect strong execution across our businesses through an unprecedented environment.

Regarding our segments, I'll first comment on Evernorth. Fourth quarter 2020 adjusted revenues grew to $30.5 billion and adjusted pretax earnings grew to $1.6 billion. Evernorth's strong results reflect organic growth with outstanding client retention and new partnerships, effective execution of supply chain initiatives and continued strong performance in Accredo, our industry-leading specialty pharmacy.

During the quarter, we fulfilled 388 million adjusted pharmacy scripts, a 19% increase over fourth quarter 2019. Overall, Evernorth delivered a strong fourth quarter as we completed our integration efforts, and we entered 2021 with good momentum.

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Turning to U.S. Medical. Fourth quarter adjusted revenues were $9.7 billion, and adjusted pretax earnings were $328 million. These results reflect COVID-19 related impacts and the return of the health insurance tax. COVID-19 related impacts in the quarter include the direct cost of COVID-19 testing and treatment, the cost of actions we have taken to support customers, providers and coworkers and decreased specialty contributions, partially offset by a reduction in non-COVID utilization. As we progressed through the fourth quarter, we experienced an increase in direct COVID-19 costs for testing and treatment as incidence rates spiked across the country. While we also saw increased levels of care deferral for non-COVID costs during the latter part of the quarter, the direct COVID-19 cost outweighed the impact of lower non-COVID costs.

Turning to membership, we ended the year with 16.7 million total medical customers. This represents less than a 0.5% decline sequentially, excluding the loss of a 240,000 life client as expected due to an acquisition, as our book of business remains resilient. We finished the year with 18% Medicare Advantage customer growth and delivered mid-single-digit growth in the Select and International segments despite a challenged economic backdrop.

Overall, results for Cigna's U.S. Medical segment reflects strong fundamentals and the impact of the increase in direct COVID-19 costs as we progressed through the fourth quarter.

In our International markets business, fourth quarter adjusted revenues were $1.5 billion. And adjusted pretax earnings were $91 million, reflecting the cost of actions taken to support customers and coworkers and investments in the business for future growth.

For our Group Disability and Other operations segment, fourth quarter adjusted revenues were $1.3 billion. Fourth quarter adjusted pretax earnings for this segment were $11 million, reflecting elevated life claims related to the pandemic and unfavorable disability claims. As previously noted, we completed the sale of the Group Disability and Life business to New York Life on December 31, 2020.

For our corporate segment, the fourth quarter adjusted loss of $381 million reflects lower interest expenses due to lower levels of outstanding debt.

Overall, Cigna's 2020 results reflect focused execution across each of our businesses through a dynamic environment as we continue to meet the needs of those we serve while delivering strong financial results.

As we turn to 2021, we have entered the year with strength and momentum, driven by our strategic actions in 2020, which David detailed. And we expect the environment in 2021 to continue to be dynamic, presenting both challenges and opportunities for our business.

Before going to our detailed outlook, with the sale of our Group Disability and Life business, contributions from Group should be removed for the purposes of year-over-year comparisons.

With that, for full year 2021, we expect consolidated adjusted revenues of at least $165 billion, representing growth of approximately $10 billion after adjusting for 2020 Group revenues. We expect full year 2021 consolidated adjusted income from operations to be at least $6.95 billion or at least $20 per share. This is inclusive of an expected COVID-19 related headwind of approximately $1.25 per share.

In 2021, we expect elevated medical costs including the impact of direct COVID-19 related costs and more normalized non-COVID utilization, and we expect impact of a gradual economic recovery on our customer base in 2021.

Given these COVID-19 dynamics, we expect the primary impact to be in our U.S. Medical business. Further, we expect the COVID-19 headwind to be more concentrated in the first quarter of the year. And so we would expect the cadence of earnings per share in 2021 to be more weighted to the final 3 quarters of the year. Specifically, we expect approximately 20% to 22% of 2021 earnings per share to emerge in the first quarter of the year.

For 2021, we project an expense ratio in the range of 7.5% to 8%. And a consolidated adjusted tax rate in the range of 22.5% to 23.5%.

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I'll now discuss our 2021 outlook for our segments. For Evernorth, we expect full year 2021 adjusted earnings of at least $5.6 billion. This represents year-over-year growth of at least 4%. In Evernorth, we expect the 2021 quarterly earnings cadence to be directionally in line with 2020. For 2021, we expect adjusted pharmacy scripts of at least 1.55 billion scripts, and we see significant opportunity to bring new innovative solutions to market through Evernorth. With less than 15% of our Evernorth revenues derived from Cigna's U.S. Medical business, we have a significant external customer and client base, and we expect continued attractive growth through existing and new Evernorth relationships.

For U.S. Medical, we expect full year 2021 adjusted earnings of at least $3.8 billion. This outlook reflects focused execution in our businesses, driven by organic customer growth, deepening of customer relationships and disciplined expense management. This outlook also includes the projected impact of COVID-19. As I said earlier, the COVID-19 headwind primarily impacts our U.S. Medical business, with the greatest impact in the earlier part of 2021.

Key assumptions reflected in our U.S. Medical earnings outlook for 2021 include the following: regarding total medical customers, we expect 2021 growth of at least 325,000 customers. This includes continued organic growth throughout the year in our Commercial business, led by the Select and Middle market segments, partially offset by lower National accounts enrollment. We also expect Medicare Advantage customer growth in our target average annual growth range of 10% to 15%, and we expect growth in our individual ACA business, which will be largely offset by our exit of our legacy non-ACA individual market offerings.

We expect the 2021 medical care ratio to be in the range of 81% to 82%, reflecting the impact in 2021 of elevated medical costs, including the impact of Direct COVID-19 related costs and more normalized non-COVID utilization, the repeal of the health insurance tax effective for 2021 and continued focused execution and delivery of strong clinical quality across our U.S. Commercial and Government businesses.

We also expect continued contributions from International Markets as we continue to deliver differentiated solutions that improve the health, well-being and peace of mind of those we serve in our global markets.

Regarding interest expense, we expect costs of approximately $1.3 billion pretax in 2021. All in, for full year 2021, we expect consolidated adjusted income from operations of at least $6.95 billion or at least $20 per share. Overall, these expected results reflect the differentiated value, strength and strategic positioning of our businesses as we deliver growth while navigating the headwind associated with COVID-19.

Now turning to our capital management position and outlook. We expect our businesses to continue to drive exceptional cash flow with strong returns on capital, even as we continue reinvesting to support long-term growth and innovation. In 2020, we deployed $4.7 billion to repay debt, and we repurchased 21.9 million shares of stock for $4.1 billion. We ended 2020 with a debt-to-capitalization ratio of 39.5%, an improvement of 570 basis points over year-end 2019, as we met our deleveraging target of a debt-to-capitalization ratio of less than 40%.

Now framing our capital outlook for 2021. We entered 2021 with $2.5 billion of deployable capital from our strong cash flow generation in 2020 and the remaining proceeds of the Group sale, net of the expected debt repayment we announced on deal close. For 2021, we expect at least $7.5 billion of cash flow from operations, reflecting the strong capital efficiency of our well-performing businesses. Combined, this gives us at least $10 billion to deploy in 2021 and positions us well to execute against our 2021 capital deployment priorities.

First, we expect approximately $1 billion in tax payments and expenditures resulting from the Group sale. We also expect to deploy approximately $1 billion to capital expenditures, primarily focused on technology to drive future growth. We expect to deploy approximately $1.4 billion to shareholder dividends, in line with our January quarterly dividend announcement. And we expect to largely deploy the remaining $6.6 billion for share repurchase and strategic M&A. Year-to-date, as of February 3, 2021, we have already repurchased 4.2 million shares for $906 million.

For the purposes of planning and 2021 earnings per share guidance, our outlook reflects the deployment of the vast majority of the $6.6 billion to share repurchase. Regarding M&A, we look for opportunities that are both strategically and financially attractive, and we would evaluate a given opportunity on its merits. Our balance sheet and cash flow outlook remains strong, benefiting from our highly efficient service-based orientation that drives strategic flexibility, strong margins and attractive returns on capital.

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So to recap, our full year 2020 consolidated results reflect strong execution led by our Evernorth segment. We entered 2021 with momentum, and we are confident in our ability to deliver our full year 2021 earnings outlook. Further, we've strategically positioned our businesses to leverage our growth framework and to be service-based and capital-light. This positioning drives significant financial strength and flexibility and gives us continued confidence in our long-term growth targets.

With that, I'll turn it over to the operator for the Q&A portion of our call.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Gary Taylor with JPMorgan.

Gary Paul Taylor - *JPMorgan Chase & Co, Research Division - Analyst*

Appreciate the details. I just want to go back to sort of thinking about the COVID headwinds this year, and I know '22 is a far way away. But from this distance, should we be thinking about $20 plus $1.25 and then including your long-term growth rate on that. Is there any reason not to sort of generally be thinking about that as the setup for 2022?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Gary, it's David. As Brian noted, we estimate the $1.25 headwind for 2021. Big picture, we think you should view it as transient or removable. I caution you from at this early stage penciling all of it as an immediate return in 2022. But to be very clear, we do believe it is removable or recoverable from that standpoint through a variety of forces. One, obviously, the effectiveness and the ramping of the vaccine that will transpire from that standpoint; two, further evolution of both programs and services as well as treatments and therapies relative to dealing with COVID; and then third, ultimately, if necessary, pricing actions and activities. So big picture, I agree with your conclusion. We just caution you not to harden it fully 100% into the 2022 number yet.

Operator

Our next question is from Kevin Fischbeck with Bank of America.

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

Okay. Great. I guess, the dynamic that you saw in Q4 around elevated medical costs, kind of more than offsetting the decline which is a little bit different than what we've seen in some other companies. But I guess, directionally similar with commentary about the impact of Commercial versus Medicare. I guess maybe since you are kind of more commercially focused, maybe you could help draw a little bit of a distinction between how you expect utilization in the Commercial business to rebound in 2021? Is there a less pent-up demand than what you might see in the Medicare business? And therefore, Commercial gets to more normal more quickly in 2021 than other business lines? I just wanted to hear your thoughts on that given your performance versus your peers in Q4.

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Kevin, it's Brian. So just a few kind of framing comments, and then I'll get to the core of your question. Throughout 2020 as the pandemic emerged, we certainly did witness an inverse relationship between COVID-19 claims and deferred care. And you step back all the way in the second quarter

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of 2020, the impact of care deferrals more than outweighed the direct costs associated with COVID-19 claims for testing and treatment across both our Commercial and Medicare businesses.

During the third quarter, these factors approximately offset one another, meaning the cost of COVID claims approximately offset the effect of care deferrals. In the fourth quarter specifically, as the back half of the quarter emerged, we started to see the cost of COVID-19 claims for both testing and treatment start to exceed the benefits we were seeing from increased care deferral activity. And so we ended the quarter with performance of medical costs in aggregate that was modestly above our seasonal baseline. That effect was consistent across both the Commercial and the Medicare books of business, although I would note that the Commercial care deferrals were lower than the Medicare care deferrals that we saw in the fourth quarter.

So that's the way I'd encourage you to think about it. And as we roll that forward into 2021, our guidance contemplates the respective books of business in the $1.25 headwind.

Operator

Our next question is from Matt Borsch with BMO Capital Markets.

Matthew Richard Borsch - *BMO Capital Markets Equity Research - Research Analyst*

Maybe if I could just ask a question on that prior dialogue. So do I have it right, maybe in Medicare, you're actually seeing the direct cost of COVID as higher than the deferral in the fourth quarter? And if so, do you expect that to continue into 2021?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Matt, it's Brian. So yes, you have that right. For the fourth quarter, we did see the direct cost of COVID-19 testing and treatment exceed the benefits of care deferral for the quarter in aggregate, with the back half of the quarter, where the acceleration really occurred. I would note, though, that the fourth quarter also saw elevated care deferral relative to the third quarter in Medicare. And again, as we roll that forward, stepping into 2021, we've assumed that the first portion of the year, there will be elevated medical cost experience in our book of business across U.S. Medical. And as the year unfolds, that will gradually dissipate towards the back half of the year.

Matthew Richard Borsch - *BMO Capital Markets Equity Research - Research Analyst*

Yes. And sorry, so just one clarification. I'm trying to isolate Medicare -- not looking for any specific guidance, but directionally, Medicare, just Medicare to understand in that book in the fourth quarter, it was -- the deferrals were less than COVID treatment costs and if that's expected to continue this year?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

In the fourth quarter, both our Commercial and Medicare businesses in aggregate, saw total claim costs that were modestly above the seasonal baseline.

Operator

Our next question comes from Ralph Giacobbe with Citi.

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Ralph Giacobbe - *Citigroup Inc., Research Division - Director and Co-Head of Americas Healthcare Research*

Last year, you had talked about a potential opportunity to go back to customers and maybe take some risk off the table for them for 2021. I'm not sure if that program resonated or not and whether that had any impact on the guidance. And maybe if there are considerations around your Stop Loss book, specifically for this year that we need to consider in terms of what's baked into the guidance?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Ralph, it's David. I think what you're reflecting back on as the pandemic, the breadth of magnitude of it began to take hold and become obvious, we made the decision as an organization that we would seek to return all the favorable economics that were manifested because of COVID disruption to clients, customers, patients, our provider partners and our coworkers. So you're reflecting back to that. We did take proactive action throughout the course of the year to work with clients. That's a client-by-client set of actions depending on the client's position, desire, funding mechanisms, et cetera, to both return value in an absolute sense. And in some cases, restructure programs with an eye toward 2021. In some cases, you could think about the, call it, the risk-sharing relationship with those clients may have moved somewhat depending again on the client's preference. But that's, again, a client-by-client call.

For the latter portion of your comment, I would say there's no meaningful difference between Stop Loss, either structure or performance expectation for 2020 versus 2021, and we continue to feel very good about the way Stop Loss is performing for peace of mind for our clients as well as for ourselves.

Operator

Our next question is from Robert Jones with Goldman Sachs.

Robert Patrick Jones - *Goldman Sachs Group, Inc., Research Division - VP*

Maybe just on Evernorth in the guidance. If I look at this $5.6 billion of operating profit expectation, it doesn't seem like it bakes in too much underlying growth if I'm thinking about this right. So I just wanted to talk through some of the pieces. If you account for the expected benefit from the Anthem overhead cost rolling off, some of the incremental deal synergies, the prime scripts. Just want to make sure I'm thinking about the underlying business there correctly. And what you guys are assuming the kind of organic underlying growth could be in this business for '21?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

It's David. So let me start, I'll ask Brian to add some additional specificity. Stepping back relative to the Evernorth platform, we're delighted. We're really pleased with the performance, the growth that is being realized because of the value that's being delivered to our clients, our commercial clients, our health plan clients, our government clients from that standpoint.

Two is, to put a pin in it, specifically relative to stranded overhead, we were able to more rapidly accelerate the extraction of the stranded overhead, largely because of executing our efficiency initiatives, but also the significant growth. So the stranded overhead extraction was more accelerated from its initiation in 2019 through 2020.

Third point, before I hand it over to Brian, I would just ask you to recognize the fact that we continue to invest significantly because of the rate and pace of growth in the business as we are continuing to add significant business to that portfolio. And we've called out before investments that are being made relative to OPEX, largely operating expenses, to add our first phase of our Prime relationship. Now we're evolving a second phase of the Prime relationship, and we're delighted to do so, and that will take place throughout the totality of 2021, all reinforcing the growth in the underlying strength.

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Meanwhile, successfully continuing to grow earnings, in line with our prior strategic target, we will look forward to providing you some additional insight relative to the forward-looking both revenue and earnings trajectory of that business at our Investor Day.

Brian, some adds?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

The only comment I'd add on top of that is to remind Robert, that the 2020 performance when you exclude transitioning clients, showed 20% revenue growth in Evernorth and 22% growth in adjusted pharmacy scripts year-on-year. So we're coming off a very strong year in 2020 and stepping into 2021 with continued momentum.

Operator

Our next question is from Justin Lake with Wolfe Research.

Moving on to our next question from George Hill with Deutsche Bank.

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

I guess as we think about the $1.25 headwind for calendar '21, are you able to give us an order of magnitude on what is the -- like the gross impact of the COVID headwind versus the gross impact of the expectation for reduced medical claims or reduced medical costs? That would be helpful.

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

George, it's Brian. So I appreciate the question and the nature of the way you structured it. I'm going to approach it maybe a little bit differently, but hopefully, this will get at what you're looking for here. As we dimensioned the $1.25, I would encourage you to think about it in 3 broad categories. The first one being the impact of elevated COVID-19 testing treatment and vaccination costs as well as some of the pressure we anticipate on our revenue, for example, in our Medicare business. I would size that at about half of the $1.25 impact as it relates to the 2021 effect on our U.S. Medical book. And you'll see that primarily in the medical care ratio or the MCR.

The second component that's sizable is in customer volumes, again, specifically in our U.S. Medical business. We would expect about 35% to 40% or so of that $1.25 to show up in the form of lower volumes due to the ongoing economic pressures associated with the pandemic. And then the balance is smaller components that will show up in different parts of the company.

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

Okay. And maybe a quick follow-up. Is there any impact expected to the Evernorth segment?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

The Evernorth impact is quite modest. And I would characterize it as immaterial relative to the size of that business.

Operator

Our next question is from Ricky Goldwasser with Morgan Stanley.

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Moving on to our next question from A.J. Rice with Crédit Suisse.

Albert J. William Rice - *Crédit Suisse AG, Research Division - Research Analyst*

Just to ask about Evernorth, 2 aspects there. One, with now enhanced the capital for deployment, it seems like part of the story for Evernorth is diversifying the service offering beyond the pharmacy benefit focus that it currently has. Can you comment on how quickly? And you think you can diversify? And what are -- maybe update us on the areas that you're thinking about adding to the capability there. And then just based on Evernorth, there was some talk last year that the PBM selling season, people were renewing for a year because of the pandemic and do you expect the selling season to have more RFPs than normal this year? Or is it sort of a normal RFP season from what you're seeing so far?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

A.J., it's David. Relative to your first question, the platforms that we are operating within Evernorth, and again, we'll walk through it in some good detail at our Investor Day.

There are 4 platforms within that portfolio. Our well-performing pharmacy services, our care management, our benefit management, and our health intelligence platforms that are functioning, operating, delivering significant value today. Each one of which will continue to be invested in, first and foremost, organically. Brian referenced the CapEx deployment that we have within our portfolio, and Evernorth is a part user of that $1 billion CapEx.

Secondly, through partnerships, the way we work to partner in different ways, shapes and forms. And thirdly, potentially through M&A from that standpoint. But the platform we have, we feel quite good about. As an illustration in terms of the M&A capabilities, we've talked about expanding our ability to serve customers where they are and where they seek to be served, whether that's expanded virtual platforms, expanded in home capabilities, et cetera, through that lens.

As it relates to your second question, the selling season, et cetera, grounded in the comments we made relative to just the very strong growth results we've put up over multiple years now. We'll be able to carry that momentum through 2021. We're pretty thick into the 2022 selling season right now. The health plan season is far along. The large commercial season is meaningfully along. And the -- we'll call it the middle market consortium selling season is in the early stages.

As of right now, we know we have 2 health plan losses for 2022. We've had essentially 99% plus retention up until that point for our health plan business, and we would like to retain every client every day. And we know that that's not possible, but we have 2 known losses that have been written about in the marketplace. Notwithstanding that, we have visibility to meaningful new business adds from the 2022 selling season, and we'll be able to continue to build on the momentum we posted for 2019 and 2020.

Operator

Our next question is from Dave Windley with Jefferies.

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

I'm hoping to hear, David, how central and important telemedicine is to Cigna and Cigna's strategy, thinking about how are you baking that into product design? How are you thinking about extended higher reimbursement, deferral of patient co-pay? And does like remote passive digital monitoring of high-risk patients fold into that picture. I'd just love to hear you talk about how central that is and how much say Cigna is pushing that as opposed to waiting on customers to pull that from you?

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David Michael Cordani - *Cigna Corporation - President, CEO & Director*

So it's interesting the way you end it in terms of push, pull. We've talked before around our orientation as being -- we think about ourselves as a consultative solution provider. So I pause a little bit on the push side of the equation. But stepping back, your framing, I think, is quite healthy.

As I noted in my prepared remarks, we see the change in which care will be accessed and coordinated is one of the 3 defining trends over the decade in front of us, and we see significant opportunity, to be clear. So let me repeat that, we see significant opportunity to deliver more value, more choice, more simplicity, with appropriate coordination back to customers and patients through effective use of virtual programs.

This is well beyond telemedicine, it's well beyond urgent care triaging. There's longitudinal nature that is attached to that. It is aided by remote monitoring. It is aided by a coordinated system to make that longitudinal delivery work. We see this transcending from health care through behavioral health to coordinated health care and behavioral health services from that standpoint. And we see it as a significant opportunity. I'd also note that we've been mindful in terms of the positioning of the corporation, whereby we see that as not only a significant opportunity in the market, but for us because we've sought not to be positioned in, we'll call it bricks-and-mortar delivery or fixed delivery infrastructure, but having the flexibility of the variable delivery infrastructure that is aided for clients.

And then lastly, we do see your point, you have the ability to design benefits. You can have a virtual primary benefit structure that are being tested in the marketplace today, and you could push that -- you can put that in the push category, but it's a choice that you would offer and we've already seen some positive markers. So a significant opportunity, our company is positioned to pursue it, and you should expect us to spotlight this in a little bit more detail on March 8.

Operator

Our next question is from Justin Lake with Wolfe Research.

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

Can you hear me this time?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Yes, we can, Justin.

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

Sorry about that. So a couple of quick numbers questions. One, the Evernorth revenues were materially higher than at least I was modeling, yet it didn't seem to flow through to the bottom line in terms of earnings, which were more in line. So curious there, if there's anything I'm missing? And then on the exchange business, can you give us an update there's a lot of competition there? I know you're rolling into a bunch of new markets. Can you share with us how much new membership you expect to have there? And any kind of margin impact kind of versus typical targets that we should think about for '21?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Justin, it's Brian. I'll take the first part of your question, and David will comment on the individual exchange part. Yes. In terms of the Evernorth business, really pleased with the revenue performance that we drove in 2020. And your comment about the relationship to the earnings, couple of things I would keep in mind there. One is the relationship that came out with Prime Therapeutics, effective April 1, and that became expanded on January 1, 2021. When we onboard any new client, there's a level of start-up cost associated with that as we think about bringing on new

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headcount to make sure that we're ramped up for the volumes that will come. So we had a little bit of expense related to the start-up associated with our relationship with Prime Therapeutics in 2020.

Additionally, the Cigna U.S. Medical in-sourcing, which is now complete, brought revenue but de minimis earnings contribution in 2020 to Evernorth. So those are really the 2 dynamics that caused a little bit of the revenue versus our earnings growth difference that you cited.

David, anything you want to call out relative to the individual business?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Sure, Justin, relative to the business. First, we're pleased with the performance that we're stepping into 2021 with relative to that portfolio. As I noted in our prepared remarks, we're expanding the counties we're participating in by about 50%. Brian did also note that we're exiting the non-ACA portion of that business. As it relates to margins, Justin, I would remind you, we were early to note that a couple of years ago, we thought that, that portfolio of businesses nationally was earning margins above a sustainable margin threshold, and we set targets to revert to a sustainable margin threshold. And in fact, the MCR we posted this year, we indicated it would show some impact of the margins more normalizing, and that indeed did take place. As it relates to the 2021 and our early look at beyond positioning, we think that our margin targets are sustainable given our provider relationships and our service proposition, and we look to grow that portfolio.

Operator

Our next question is from Steven Valiquette with Barclays.

Steven James Valiquette - *Barclays Bank PLC, Research Division - Research Analyst*

So as we think about the Commercial membership outlook, you mentioned you expect continued organic growth throughout the year in overall Commercial membership. Curious if we can read into that, maybe that Cigna has perhaps already troughed on the quarterly progression of Commercial enrollment as it relates to COVID impact, economic impact, et cetera? And then just within that, with National accounts expected to be down a little bit. Any sense on when we may see the trough on that, whether it's early in the year or late in the year in 2021?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

It's David. I think you've identified several important features there. So as it relates to Commercial customers for 2021, we -- as expected, we expect it to step into 2021 with about the number of customers we would end 2020 with. As it relates to the year's pattern, I'd ask you to think about it as follows. First, we expect the ongoing COVID impact to disenrollment to continue to have pressure on customers throughout the first half of 20 -- our customer number throughout the first half of 2021. Second, as typically takes place in the National account segment, there are some non-COVID related disenrollment that happened historically in that business because most of the selling takes place during the first portion of the year.

Offsetting that is continued growth and strength in the Select segment that has a very active selling season throughout the course of the year as well as some known we'll call Middle market, new business adds that will take place during the middle portion of the year.

Now as it relates still looking forward to U.S., the final part of your question relative to the trough on National accounts. Our early look at 2022 is we would expect a very attractive retention number at this point for our U.S. Medical National account relationships as well as the selling season has been pretty active right now for us. The RFP volume is up, the quality RFP volume is high. We have some new business opportunities, wins that we have on board already, and we're in active pursuit. So we have a level of optimism relative to the outlook for that segment for January 2022. I hope that helps, Steve.

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Operator

Our next question is from Ricky Goldwasser with Morgan Stanley.

Moving on to our next question from Josh Raskin with Nephron Research.

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

Congrats to Eric and Brian and the rest of the team on the new roles. So our question here is more around Cigna was relatively early in sort of that development of an ACO strategy. It seems like the market's certainly been catching up quickly. So was wondering if you could speak to your efforts around engaging providers, especially primary care physicians and maybe perhaps how that approach differs in your Medicare book versus your Commercial book?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Josh, so relative to the ACO strategy, I think it's a broad definition of what the market calls value-based relationships. And you're correct, we had an early start and a lot of passion and drive and therefore, strategic direction relative to it. I would start with the end, and that is the Medicare Advantage book, in general, has a higher penetration of and comprehensive nature of value-based care relationships per customer that we serve versus Commercial. So -- and you probably see that in other ways, you look at the marketplace. The primary care physicians, the integrated multi-specialty physician groups, et cetera, tend to adopt, adapt and internalize value-based care more comprehensively for Medicare Advantage given that population's health needs and the opportunity to deliver really significant value.

The exciting end piece of it is we've been working now for a decade to prove that thesis in the Commercial space. And it varies by market in terms of the level of breadth and depth. But we have well in excess of 600 collaborative accountable care relationships that are up and running and delivering meaningful value, the more mature ones are delivering meaningful value for customers and clients. What does that mean? Clinical quality to higher gaps in care closure, service quality, strong service experience and improved affordability from that standpoint.

And the last comment I would add here is the market is always dynamic. But one of the impacts of COVID-19 is that it jars everybody in every norm. And as it relates to value-based care, it puts a spotlight back on value-based care, that shared risk insured performance relationships now may look a little bit more palatable to some that may have not viewed it in the past and were more weighted to a fee-for-service model. So we see an opportunity to further expand and deepen some of those relationships, both in Commercial, specifically, but as well as in some of the Medicare Advantage opportunities.

Operator

Our next question is from Charles Rhyee with Cowen.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

Just wanted to ask again about the direct COVID cost in this year in this $1.25. And I apologize if you gave it, but is there a way to give a split between maybe testing costs relative to treatment costs in that number that you expect this year? And I think there's been some talk about potential for changing rules where plans would be required to cover additional testing costs, like about return to work kind of a cost that I think plans are currently covering. Just wanted to get your sense first on that first part. And then secondly, is that a big amount that you -- if that were to happen, how big amount is that in the testing scheme overall?

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Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Charles, it's Brian. So in terms of the first part of your question there, dimensioning the testing versus the treatment, we've gone through extensive modeling, as you might imagine, to project what we think is going to transpire in 2021, which led us to $1.25 COVID impact that I described earlier. And as I went through to a previous question, we expect about half of that to come through in the form of elevated claim costs and/or revenue pressure in our U.S. Medical MCR book. So I'm not going to split apart each of the different components in that for you, but just rest assured, we've got a variety of projections that underlie that. So David, maybe you want to comment on the effects?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Sure. Relative to the testing, as we stand today, first and foremost, the industry, broadly speaking, stepped in early, clear and aggressively in support of clients and patients relative to testing initially, as well as evolving thought process and procedures relative to treatment. As it relates to what I would describe as OccMed or worksite support, the posture has been thus far and good collaboration with HHS administration staff that is outside of what an insurance or a service relationship should be. To the extent it's revisited, we revisit it dynamically, but that's typically carried by the employer through an OccMed relationship or otherwise. I'd also remind you that 85% of our Commercial business is self-funded. So we act as a fiduciary. And in cases where individual employers want assistance relative to that, we're proactively supporting through that lens. But we do not see that as either: a, likely in the immediate future, even relative to engagement on these topics this week; or b, a needle mover for us given the makeup of our portfolio of businesses.

Operator

Our next question is from Lance Wilkes with Bernstein.

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

So let me just follow-up a little bit on the strategic capital deployment. And if you could just talk to maybe 2 dimensions on that. I appreciate your earlier comments. As you were talking about bricks-and-mortar being of less interest and specifying some of the areas in virtual home and remote monitoring, et cetera, that were of interest. If maybe you could just call out the distinction, maybe I'm putting too much emphasis on physician practices being bricks-and-mortar and excluding them as an area of focus.

And then similarly, if it's in Evernorth, will it be more focused on providing these services to employers and health plans? Or how much of the focus is providing these services to risk-bearing primary care or other value-based care sorts of companies?

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Lance, it's David. I'll start with the latter portion of your question first. So as we evolve our capabilities, both the present state but evolve our capabilities, you should think about, in general, all that happens within Evernorth. And it happens within Evernorth as it relates to a platform of services to serve health plans, to serve corporate clients, to serve governmental agencies and to offer services to, as you articulated, risk-bearing or performance-based health care delivery systems.

And you should think about Cigna, Cigna's U.S. Medical portfolio as a consumer of those services. Now clearly, an important development partner, but a consumer of those services as another client of Evernorth. As it relates to the first portion of your question, I think your basic framing of it is right. And so if we just reiterate it and step it up a notch. Our view is that the U.S. is not in need of more physical proximity and physical plant to serve the population in general. Especially in urban and suburban areas, we obviously have additional need states relative to rural areas from that standpoint.

Secondly, that consumer behavior in a variety of areas, including health care, has reinforced a desire, not an acceptance, but a desire for bringing care and services to me in a real-time basis in a highly personalized basis. Therefore, virtual care coordination. And obviously, that's augmented

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with clinical staff, but it's bringing the service to the individual in an immediate real-time basis, so long as it could be longitudinally managed and coordinated effectively.

And then the last point I want to be really clear on our view of it is as a complementary aspect to the care delivery system, not as a disintermediation play. But it's a complementary aspect because to make it work properly, it needs to be connected back into the health care delivery system. And we have many examples of it working today in our approach to virtual, both for medical as well as behavioral health. We just see the ability to ramp it significantly given both the demand and the acceptance, and then the tool availability.

Operator

Our last question will come from Scott Fidel with Stephens.

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

Okay. I had a question just maybe helping us to think about the Medicare Advantage margin progression that you're thinking about for 2021 and 2022? And particularly, maybe if you can call out, I don't know, maybe within that $1.25 headwind from COVID, just how you're -- what you're thinking specifically about the impact from the lower RAFs in 2022, which I guess would probably impacting you a bit more just because of all the enrollment growth, the 18% growth that you had in MA just last year. But then as we go into 2022, how much sort of improvement in margin you could potentially get as you normalize the RAFs? And then also, it looks like you have a pretty solid base rate update from CMS as well in terms of that 4% plus?

Brian C. Evanko - *Cigna Corporation - Executive VP & CFO*

Scott, it's Brian. So a few components to your question there. And just broadly, the way I would encourage you to think about it is we're on a multiyear growth journey for this business, right? We're year 2 of our geographic and product expansion with the expectation of 10% to 15% annual growth, really happy with the 18% growth we put up in '20 and well on track to achieve 10% to 15% in '21.

The margin profile tends to vary for a few different reasons. One is when we go into a new market, there tends to be a buildup in terms of investments in people and in marketing before the customers start to come in. Two is, when we write a new customer, typically, there's a bit of a ramp relative to profitability from a durational standpoint due to the risk adjustment coding, which you appropriately called out. Thirdly, due to the unique nature of 2020 and the COVID-19 headwinds that we faced, there was lower utilization, right? So as a result of that, we were not able to get all of the risk adjustment codes that we would in a normal year, if you will. We factored all that into the 2021 outlook, the $1.25 earnings per share headwind that we've called out here. A component of that is associated with Medicare Advantage, and it's associated with lower revenue than we would have otherwise anticipated having. So as you kind of step forward, as David said in the beginning, 2022 and thereafter, we expect some of that will work itself out. And we're not going to give you exact 2022 guidance here today. That's the way I would encourage you to think about the margin profile.

Operator

I will now turn conference back over to Mr. David Cordani for closing remarks.

David Michael Cordani - *Cigna Corporation - President, CEO & Director*

Thank you. So just to wrap up, I'd like to highlight a few key points from today's discussion. First, I'm very proud of the way in which our colleagues supported the needs of our stakeholders throughout this pandemic, while also ensuring that we delivered on our shareholder commitments. We delivered solid 2020 financial results, including revenue and EPS growth and outstanding free cash flow. And our strong 2020 performance and

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the strength of our businesses, give us confidence that we will achieve continued attractive growth in 2021 and beyond, driven by significant increases in revenue, ongoing profit growth and very attractive cash flow performance.

We thank you for joining our call today, and we look forward to going into more depth with you around our growth plans at our Investor Day, which is slated for March 8. Have a good day.

Operator

Ladies and gentlemen, this concludes Cigna's Fourth Quarter 2020 Results Review. Cigna Investor Relations will be available to respond to additional questions shortly. A recording of this conference will be available for 10 business days following this call. You may access the recorded conference by dialing (866) 451-8962 or (203) 369-1203. There is no passcode required for this replay. Thank you for participating. We will now disconnect.

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