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CI.N - Q3 2021 Cigna Corp Earnings Call

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OVERVIEW:

Co. reported 3Q21 adjusted revenue of $44.3b, after-tax adjusted earnings of $1.9b and adjusted EPS of $5.73. Co. expects full-year 2021 consolidated adjusted revenue to be at least $172b and Full-year 2021 adjusted EPS to be at least $20.35.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by for Cigna's Third Quarter 2021 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 Principle 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 third quarter 2021 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

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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.

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 third quarter, we recorded an after-tax special item benefit of $35 million or $0.10 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.

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 dividends, and does not assume any impact from any business combinations or divestitures that may occur after today, such as our recently announced planned divestiture of Life, Accident and Supplemental Benefits Businesses outside of the U.S., which we expect to close in 2022.

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

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

Thanks, Alexis, and thank you to everyone for joining us on our call today. This morning, I'm going to spend a few minutes talking about our strong results for the quarter, how we are advancing our growth strategy, and I'll provide some additional perspective on our 2022 outlook. And then Brian will share some more details about our third quarter results and our outlook for the remainder of the year, and then we'll take your questions.

So let's jump in. During the quarter, we delivered adjusted revenue of $44 billion and adjusted EPS of $5.73 per share, all while continuing to reinvest back in our business to fund growth, expansion and ongoing innovation, and we continue to return significant value to our shareholders.

These results reinforce we are delivering for our customers, our patients, clients, provider partners, as well as for you, our shareholders. With our high-performing health service portfolio and sharp focus on executing our strategy, we are confident in our ability to continue driving growth and are again raising our full year 2021 guidance for adjusted EPS and revenue. Our performance is strong, considering the ongoing impact of the pandemic on medical costs, as well as the higher claims we've experienced amongst the Special Enrollment Period or SEP customers within our Individual business.

As it relates to our MCR in the quarter, our Commercial business did improve from the second quarter to the third quarter, and our Medicare Advantage business also improved sequentially. We continue to execute a series of actions in 2021 and 2022 to further improve our MCR, and Brian will walk through this in more detail in a few moments.

Separately, in early October, we also announced an agreement with Chubb to sell our Life, Accident and Supplemental benefits business in our International Markets platform in 7 countries for $5.75 billion.

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We expect to realize about $5.4 billion in net after-tax proceeds and to complete the transaction in 2022 following regulatory approvals. Guided by our strategy and similar to our 2020 divestiture of our Group Insurance business, this transaction unlocks the value of a best-in-class leading asset while also enabling us to even more sharply focus our business on health and well-being services.

So overall, our performance for the quarter reflects our clear strategy and strong execution in delivering attractive results, and importantly, our ongoing commitment to prioritize and support the evolving health and well-being needs of those we serve.

Now I'll walk through some additional detail for our Evernorth and U.S. Medical businesses. A year ago, we launched Evernorth into the marketplace as our health service platform, focused on servicing health plans, employers, government organizations and healthcare providers. Since that time, Evernorth has established itself with unique partnerships and innovative services that are resonating with multiple buyer groups.

Our Evernorth Pharmacy and our medical offerings through our U.S. Medical platform are the 2 primary gateways through which most of our clients and customers form their base relationship with us.

Wrapping around these 2 exceptionally strong platforms are our additional suites of innovative health services through Evernorth, including Benefits Management, Care Solutions and Intelligence solutions. These help us to expand and deepen existing relationships.

In the third quarter, Evernorth retained and expanded our relationship with the Department of Defense TRICARE pharmacy program and renewed a 7-year contract. It's our privilege to serve almost 10 million active duty service members, retirees and their families.

Evernorth will continue supporting TRICARE pharmacy operations, including specialty pharmacy services, military pharmacy claims and retail network pharmacies. The new contract also allows for expansion of specialty and care coordination services through 2029. As we look through the balance of the year and into 2022, Evernorth will continue to grow revenue and earnings.

Turning to our U.S. Medical platform. In U.S. Commercial, our teams are leveraging and deploying the innovative solutions from Evernorth to expand our service offerings and address the evolving needs of our clients and customers. For example, in our U.S. Commercial platform, we are leveraging Evernorth's MDLIVE capabilities to expand virtual care options for our customers through their employers with primary, urgent, behavioral and dermatology care.

As part of these value-based arrangements during virtual visits, MDLIVE physicians are leveraging our Evernorth Intelligence capabilities, enabling them to provide a more connected and coordinated experience. And we continue to expand our capabilities with MDLIVE as we recently launched a virtual first health plan for employers.

Another great example of Evernorth and U.S. Commercial partnering to bring more value to our health plan clients is a new arrangement we have with the University of Pittsburgh Medical Center Health Plan. We will make in-network care available to UPMC customers who live, work or travel outside of their network service area. UPMC has been an Evernorth pharmacy client for 16 years, and this agreement illustrates how we are collaborating across our enterprise to deliver greater affordability and differentiated value for health plan clients.

We are pleased with how the market continues to recognize the value we are delivering through our broad suite of solutions. And as such, we continue to grow through both our U.S. Commercial and Evernorth platforms.

Within Medicare Advantage, consistent with our strategy, we continue to grow in our existing markets and are expanding into new geographies. Our progress is further supported by our overall value of our offerings. For 2022 calendar year, 89% of our Medicare Advantage customers will be in four-Star or greater plans nationally. This is the highest level we've ever achieved, and it marks the fifth year in a row we've improved our Star's performance.

And in our Individual & Family Plan business, we have driven strong growth in this year, increasing customers by 47% through the third quarter. A substantial portion of this growth did come from the extended Special Enrollment Period. And as I previously noted, some of the MCR impact in

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the third quarter was driven by the medical costs amongst those we added during the outpaced SEP growth. We do expect this will moderate in 2022.

We are positioning ourselves to build on this momentum in the Individual & Family Plan business by expanding our addressable market again, as we enter in 3 new states and 93 new counties in 2022. These new markets offer the potential to reach an additional 1.5 million customers.

The continued strength of our results and the growth we are generating through the execution of our strategy gives us confidence we will deliver against our commitments in 2021. We will deliver EPS in line with our long-term targets and revenue growth well above our long-term targets for yet another year. We will also deliver EPS within our long-term target range in 2022.

Specifically for 2021, we are committed to delivering our increased guidance for full year adjusted EPS of at least $20.35. For full year 2021, we remain on track for generating at least $7.5 billion of cash flow from operations, and we expect to return more than $7 billion to shareholders in 2021 through dividends and share repurchase.

Looking to 2022, we expect to grow EPS by at least 10% off of our increased 2021 guidance of at least $20.35 per share. We anticipate a number of tailwinds, including core growth in our business, and additional contribution from margin expansion in our U.S. Medical business as we drive pricing actions, execute affordability and efficiency initiatives and benefit from the return of Medicare risk adjustment revenue to more normalized levels.

We're also expecting year-over-year headwinds as we plan for net investment income to be more in line with historical levels. And of course, the rate and pace of ongoing strategic investments will vary from year-to-year. In short, 2022 will be another strong year for Cigna.

Now to briefly summarize. As we've demonstrated through the quarter and throughout 2021, we are delivering for our customers, patients, clients, and provider partners as they experience the ongoing challenges of the pandemic. We are also taking significant value-enhancing actions such as divesting a portion of our International business, returning substantial amounts of capital to our shareholders and continuing to strategically invest in our capabilities and in strategic partnerships. All of which position us to continue to advance our long-term growth agenda and continue to deliver shareholder value.

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

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

Thanks, David. Good morning, everyone.

Today, I'll review key aspects of Cigna's third quarter results, including the ongoing impact of COVID-19 on our business, and I will discuss our updated outlook for the full year.

During the quarter, total medical costs were higher than our expectations within our U.S. Medical segment, driven largely by the impact of the Delta variant in our U.S. Commercial business and increased medical costs for Special Enrollment Period customers in our U.S. Individual business. Importantly, I would remind you that approximately 80% of our revenues are from service-based businesses that are not significantly exposed to medical cost fluctuations.

Our balanced portfolio and multiple levers for value creation resulted in Cigna's overall revenue and earnings exceeding our third quarter expectations. This strong third quarter performance, coupled with capital deployment activities, led to an increased outlook for full year 2021, which I will discuss shortly.

Now turning to Enterprise results. Key consolidated financial highlights in third quarter 2021 include adjusted revenue growth of 9% to $44.3 billion; adjusted earnings growth of 20% to $1.9 billion after tax and adjusted earnings per share growth of 30% to $5.73. Results in the third quarter reflect strong top and bottom line growth with contributions across all of our businesses, with overall performance above our expectations.

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I'll now discuss our segment level results, and will then provide an update on the details of our outlook, as well as our capital positioning.

Regarding our segments, I'll first comment on Evernorth. Third quarter 2021 adjusted revenues grew 13% to $33.6 billion, adjusted pharmacy script volumes increased 8% to 411 million scripts and adjusted pretax earnings grew 7% to $1.5 billion compared to third quarter 2020. Evernorth's strong results in the quarter were driven by organic growth, including strong volumes in retail and specialty pharmacy, along with ongoing efforts to improve affordability for the benefit of our clients, customers and patients, and deepening of existing relationships, partially offset by significant strategic investments to support ongoing growth, including our virtual care platform and technology capabilities.

Overall, Evernorth continues to create differentiated value for clients and customers, while driving overall revenue and earnings growth that exceeded our original expectations through the first 3 quarters of 2021.

Turning to U.S. Medical. Third quarter adjusted revenues were $10.5 billion, and adjusted pretax earnings were approximately $1 billion. Overall, our U.S. Medical earnings exceeded our expectations during the third quarter, reflecting the impact of favorable net investment income and increased specialty contributions, partially offset by higher claim costs due to the net impact of COVID-19 and increased medical costs for Special Enrollment Period customers in our Individual business. The net effect of these claim cost impacts produced a medical care ratio of 84.4% in the third quarter.

Looking ahead, we are actively managing overall medical costs and our MCR with a range of actions, including: continuing to leverage our insights from our strong data and analytics capabilities to address key drivers and identify opportunities such as guiding customers to more effective and efficient sites of care, continued discipline in our pricing and rate actions, and we're also continuing to promote preventative care and access to behavioral services to provide meaningful support to patients and moderate overall medical costs over the longer term.

Turning to membership. We ended the quarter with 17 million total medical customers, an increase of approximately 368,000 customers year-to-date. In U.S. Medical, the year-to-date customer growth was driven by net growth in Select and Middle Markets within U.S. Commercial and continued organic growth in Medicare Advantage and Individual within U.S. Government.

In our International Markets business, third quarter adjusted revenues were $1.6 billion and adjusted pretax earnings were $250 million. These results were in line with our expectations.

Corporate and other operations delivered a third quarter adjusted loss of $275 million.

Overall, Cigna's broad portfolio of services continues to serve the needs of our customers and clients. Cigna remains committed to delivering value for all of our stakeholders, leveraging our well-positioned businesses.

Now turning to our updated outlook for full year 2021. We are raising our adjusted earnings per share guidance for full year 2021 to at least $20.35 per share, reflecting the strength of the quarter, the favorable impact of our year-to-date share repurchase and acknowledgment of the ongoing fluidity of the broader environment. This represents EPS growth of at least 10% from 2020, consistent with our long-term EPS growth range of 10% to 13%, even with the ongoing challenges associated with COVID-19 and while having significantly increased our dividend in 2021.

As we look forward, it is clear that COVID-19 will continue to have an impact in the fourth quarter and in 2022, and as time progresses, COVID-related impacts and the ongoing performance of the business are becoming more intertwined. Therefore, we no longer believe it's instructive to continue to quantify the impact of COVID-19.

These dynamics are fully contemplated in our 2021 expectations for adjusted EPS of at least $20.35 and our 2022 expectations for EPS growth of at least 10% off this 2021 guidance.

Turning to revenue. We now expect full year 2021 consolidated adjusted revenues of at least $172 billion, representing growth of at least 11% from 2020 when adjusting for the divestiture of our Group Disability and Life business. I would note this revenue growth rate significantly exceeds our

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projected long-term average annual growth goal of 6% to 8% and represents the third consecutive year of significant revenue outperformance since our combination with Express Scripts in late 2018.

I will now discuss our 2021 outlook for our segments. For Evernorth, we continue to expect full year 2021 adjusted earnings of at least $5.8 billion, representing growth of at least 8% over 2020, reflecting the significant value we create for our customers and clients.

For U.S. Medical, we continue to expect full year 2021 adjusted earnings of at least $3.5 billion. Underlying this updated outlook, we now expect the 2021 medical care ratio to be in the range of 84% to 84.5%, which includes our expectations for elevated medical costs for Individual Special Enrollment Period customers.

Regarding total medical customers, we continue to expect 2021 growth of at least 350,000 customers.

Now moving to our 2021 capital management position and outlook. We expect our businesses to continue to drive strong cash flows and returns on capital, even as we continue reinvesting to support long-term growth and innovation. For full year 2021, we continue to expect at least $7.5 billion of cash flow from operations, reflecting the strong capital efficiency of our well-performing businesses.

Year-to-date, as of November 3, 2021, we have repurchased 26.5 million shares for $6.3 billion. And we now expect full year 2021 weighted average shares of approximately 342 million shares. This includes the impact of the $2 billion accelerated share repurchase that we announced in the third quarter.

On October 27, we declared a $1 per share dividend payable on December 22 to shareholders of record as of December 7. 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.

So now to recap. Results in the third quarter reflect strong top and bottom line growth, with solid contributions across our businesses. Cigna has shown the ability to deliver value through dynamic environments with our breadth of businesses and multiple earnings levers. We continue to support our customers, clients and coworkers and deliver on our financial commitments. We now expect 2021 full year adjusted earnings of at least $20.35 per share, representing growth of at least 10% from 2020, consistent with our long-term EPS growth rate range of 10% to 13%. And we expect to grow 2022 adjusted EPS at least 10% off our raised 2021 guidance.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Mr. A.J. Rice with Credit Suisse.

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

Just maybe to try to drill down a little bit on that expectation for at least 10% growth off the new updated numbers for this year. I know it sounds like you're getting away from talking about that $2.50 of net COVID impact that you're absorbing this year? I know there's various inputs there. But I was wondering because there -- last quarter, it sounded like you were carrying a lot of your expectation for COVID-related costs broadly defined into next year. As you think about your updated thoughts about '22, can you comment on how much of an ongoing COVID headwind are you expecting? And is there any other big changes to the puts and takes you've laid out last quarter as you think about '22.

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

It's David. Let me try to shape our insights relative to 2022 now that we're much deeper into 2021. First, you're right, earlier this year, we've tried to frame the magnitude of the headwind and indisputably, COVID had many disruptions to the marketplace, whether it was testing, treatment, revenue dislocation, et cetera.

Against that backdrop, as you know, our broad service portfolio and our broad funding mechanisms continue to perform quite well, and we're able to deliver from a marketplace standpoint. If you think about 2021, there's really 4 big chunky items: one, we'll put it in the headwind category, the headwind created by the COVID costs and the headwind created by MRA revenue decrement; and then positives offsetting that somewhat, which were favorable net investment income and some operating expense items.

Now as we think about and look at the 2022 environment, our visibility in terms of our growth outlook, our rate execution, our affordability initiatives, our efficiency initiatives and our understanding of how this year is coming to close, broadly speaking, those puts and takes in 2021 largely offset one another as we step into 2022, the headwinds and tailwinds. So our at least 10% growth in 2022 off of our elevated 2021 EPS essentially represents capital deployment in line with our strategic target of 4% to 5% of accretion, and the residual at least 5% to 6% from fundamental operating growth to get us to that at least 10%.

So to recap, additional visibility in terms of the drivers for 2022, growth, mix of growth, rate execution, affordability. And then secondly, the puts and takes in 2021 are configuring in a way that they largely offset one another as we step into 2022 underscoring that at least 10% is largely fundamental for our business portfolio.

Operator

Our next question comes from Ms. Lisa Gill with JPMorgan.

Lisa Christine Gill - *JPMorgan Chase & Co, Research Division - MD, Head of U.S. Healthcare Technology & Distribution Equity Research and Senior Research Analyst*

David, I just wanted to better understand how you're thinking about the Evernorth business as we think about 2022. I know you've talked in the past about some of the business losses, but if you can give us an update as to how to think about Evernorth going into 2022? And then as we think about the Evernorth business and think about the virtual primary care offerings that are out in the marketplace, what are you thinking with MDLIVE?

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

Good morning, Lisa. So relative to Evernorth, first as we step into 2022, as Brian and I both noted, we're quite pleased with the underlying performance of Evernorth. If you look at the inherent growth that Evernorth has delivered for the organization and the diversity of the growth, we're quite pleased with that. Secondly, our ability to both drive fundamental growth, continue to invest in innovation and extend our partnerships, we feel quite good. So just framing Evernorth and then coming to the MDLIVE question, our Evernorth portfolio has 4 specific portfolios of services that are positioned well: Evernorth Pharmacy, Evernorth Care, Evernorth Benefits and Evernorth Intelligence.

Our positioning relative to serving health plans, large employers, expanding with governmental agencies and increasingly with healthcare providers, continues to resonate well in the marketplace. For 2022, to your comment relative to some losses, we expect the retention rate in the Evernorth pharmacy business in the mid-90s, which is still a strong result even with the known losses we had identified. And given the strength we've had of growth over the last several years, we are quite committed to maintaining price discipline in the marketplace. So the business portfolio will grow yet again.

Specific to MDLIVE, we're delighted to have the MDLIVE capabilities in our portfolio, and that now resides within Evernorth Care. We see the utilization of those services continuing to grow. As I noted, beyond important, urgent or triage care, but to primary, behavioral, dermatology. And

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then we've recently expanded our virtual first offering. So we see it as a great opportunity to both expand access, improve affordability, but finally, it presents a platform to broaden some access to care in terms of alternative site care capabilities. So in a nutshell, we're pleased. We'll grow again and we're investing in further growth, including within the virtual capabilities of MDLIVE.

Operator

Our next question comes from Mr. Justin Lake with Wolfe Research.

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

I wanted to ask David about the International sale. First, in terms of a multiple, it looks like you got about 10 to 12x kind of net income for that business. Is that correct, in the right ballpark? And then if so, just curious in terms of the strategic kind of nature of the sale in terms of the multiple looks kind of depressed relative to a business that's historically looked at as a double-digit top line grower? And then can you tell us how we should think about capital deployment once you get those funds? Is it going to be similar to what we saw with the Life and Disability where there's a lot of share repo? Or should we think about something else?

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

Justin. Let me start and have Brian shape a little further, both how we feel about the value realization here and the capital deployment. First, stepping back, we're quite proud of what has been built in our International portfolio over a long period of time. This specific portion of our International portfolio, so direct individual Life, Accident and Supplemental businesses, we've successfully grown over a long period of time. But using our strategy as a guide, the important underscore here, our strategy guides us to further enhance and deepen our health and well-being solutions. This portion of our portfolio was less directly aligned over time to that. So we use the strategy as a guide, number 1.

Two, we feel very good about the value realization and the net value realization here is quite important in terms of a high-performing asset, and I appreciate your correlation to the Group transaction, another high-performing asset where we felt quite good about using our strategy as a guide and capitalizing on a very attractive valuation. And then finally, that strategic action is done to allow us to even further intensify our focus in the subsegments of the business that are more health and wellbeing-oriented, both in the U.S. as well as globally from that standpoint as we'll continue to grow.

So I'll ask Brian to speak a little bit more toward how we looked at the valuation and our capital deployment philosophy going forward.

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

Sure, David. So the math that you asked about in terms of the 10 to 12x multiple is in the right ballpark, if you're looking at U.S. GAAP earnings contributions from the divested businesses. But very importantly, this is a case where economics and accounting don't necessarily square up. If you look at the discounted cash flows of the business here, and the purchase price that we were able to get, it's quite an attractive deal economically. But we're quite pleased with the financial terms for that reason as you look at the timing of when dividends were available to be extracted, as an example.

In terms of deployment with the proceeds, the broad template, as David made reference to of our Group Disability and Life divestiture, is what we would expect to follow in this instance, as well, with the exception of we don't have the same need for long-term debt repayment as we did with the Group Disability and Life transaction. So we would expect the primary use to be for share repurchase. And when we indicated in the press release that this would be neutral, slightly dilutive to our 2022 EPS outlook, that's under the assumption that the primary use is for share repurchase.

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Operator

Our next question comes from Ms. Rivka Goldwasser with Morgan Stanley.

Michael Ha - *Morgan Stanley, Research Division - Equity Analyst*

This is Michael Ha on for Rivka. So as it relates to 2022 Commercial growth, a number of your peers have already mentioned expecting strong growth, diffused concerns around member attrition, the dynamic and emphasize share gains. I think one of your peers even mentioned '22 shaping up to be one of the strongest National account selling seasons in history.

So with that said, it's been a bright area but also hard to imagine that everyone is winning contracts and gaining share. So with that context, what are you guys seeing with the competitive landscape? And are you able to grow next year when everyone else seems to be taking share?

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

It's David. Just a minute of backdrop relative to our performance in the Commercial market and then I'll jump right into '22. We have a very focused strategy and a long track record over the last decade of successfully growing in the Commercial marketplace as we seek to subsegment and deliver the right solutions for our respective clients in that marketplace. And if you think about it over the last decade-ish, we've generally grown low single-digit medical membership, we couple that with significant and targeted cross-selling of our new and innovative services and then we complement that with appropriate pricing actions. And the net of that yields higher single-digit revenue growth. So that's the big picture of our strategic approach.

I'd also highlight with Evernorth, we are further expanding the services that we're able to bring through to deepen relationships like our prior conversation relative to virtual care as an example.

Now specific to 2022, to be clear, we'll grow again. We will clearly grow our medical customer base again. And specifically within the Commercial market, we have good visibility in terms of having net growth in our National accounts and large account business portfolio and we'll have another year of growth within our Select segment. So the net of all that, of any marketplace that is competitive as we are oriented around solutions that have affordability and high engagement programs with the right funding mechanisms, we will again have another year of net growth in the U.S. Commercial portfolio, and it's something we're quite proud of and positioned to continue on.

Operator

Our next question comes from Mr. Kevin Fischbeck with Bank of America.

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

Great. It sounds like in the quarter, you mentioned you benefited from investment income and specialty outperformance, I guess, 2 things. So do you believe that the specialty outperformance is something that is going to be sustainable? And then if you could just talk a little bit more about the competitive landscape for Commercial pricing for next year. Do you think that you're going to be within your target range, or I guess maybe where in your target range do you expect to be in the Commercial business for next year?

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

Kevin, it's Brian. I'll start on the first piece of your question. I think this was in the context of our U.S. Medical performance in terms of your question on specialty. So as you reflect on our third quarter performance for that segment and again, the earnings in totality were above our expectations in the quarter, we had 2 areas of favorability. As you called out, investment income and specialty contributions and your specialty contributions

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include pharmacy, behavioral, dental, the full suite of portfolio capabilities we have in the specialty domain. That was partly offset by the 2 sources of claims pressure that I articulated in the COVID-related pressure in Commercial as well as the Special Enrollment Period, MCRs that were elevated in the individual exchange.

Specifically on the favorability that we recorded in the third quarter, the investment income is nonrecurring. So you should not consider that to be something that would occur again in the fourth quarter or into '22. We would expect the specialty contributions to persist as favorability as we head into fourth quarter and into '22. That was a smaller component of the 2 in terms of the favorable items in the third quarter, but that is something we would expect to continue to persist going forward.

David, maybe you'll comment on the pricing environment for Commercial.

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

Kevin, relative to the pricing environment for Commercial, and I'm going to maybe sneak in a little bit on the Individual marketplace here as well, but specifically, that market has continued to be a competitive market, and it remains that, meaning the Commercial marketplace, more broadly, the employer Commercial market, and with that as a backdrop and to my prior answer, we will grow our Commercial book of business, and we will improve our MCR. Our visibility has us both growing and improving our MCR within the Commercial book of business.

So to do that, we'll be quite disciplined, Kevin, to be clear, and we are willing to make targeted trade-offs for MCR or margin versus volume. And the net of that will yield net customer growth and net margin improvement as we step into 2022.

An add-on specifically in the Individual market, our visibility in the Individual market is that there are significant pockets of competitiveness in certain markets. And as such, in the Individual marketplace, we would expect for 2022 to see no growth or more likely negative growth, some shrinkage in our book of business, but improvement in the MCR within that portfolio and that's fully contemplated in our 2022 outlook of net growth for the portfolio as well as earnings expansion.

Operator

Our next question comes from Mr. Gary Taylor with Cowen.

Gary Paul Taylor - *Cowen and Company, LLC, Research Division - MD of Health Care Facilities and Managed Care*

Just want to go back to the MCR comments, and I appreciate what you just said, David, but I just want to think a little bit more about 2021 so far. So as we kind of look at the potential impact of Special Enrollment Period enrollees based on your typical attrition, it doesn't look like that's particularly material to the increase in MCR versus 2019 baseline, which is up about 400 basis points in the 3Q, and you had a lot of COVID costs, but it was up almost 400 basis points in the 2Q, and you didn't have a lot of COVID costs and you had more deferred care coming back.

So I guess the question is, is there any other substantial moving parts to how you're running versus the 2019 baseline? And then just going forward, what are your -- what do you anticipate as COVID and the Delta variant comes down, do you feel like Commercial utilization is largely caught up or we're sort of still back in a cycle like we were in the 2Q, where you see some of the deferred care increasing?

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

Gary, it's Brian. So I'll try to take the various components of that question here. So if you think about where we're running in 2021 on the MCR, maybe I'll talk in terms of the full year guide, I think that's probably the most constructive way to pull it apart. The 84% to 84.5% refresh guidance that we issued, if the Special Enrollment Period lies within the Individual exchange portfolio had not grown to the level that they are and had not

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had the elevated MCR that they did in the quarter, we would have had an MCR performance for the full year that was more like the higher end of our prior guidance range.

So toward the higher end of the 83% to 84% range, if you exclude the impact of the Individual SEP customers from the full year outlook. So just give you a little bit of dimensioning as to the materiality there.

Those customer lives have built up over the course of the year. So there were not that many in the second quarter. There were many more in the third quarter. And the elevated MCR hit us particularly significantly in the third quarter, and we expect that pressure to continue into the fourth quarter. As David made reference to in a prior question, we would expect that to dissipate into 2022 as many of those lives attrite and/or choose new carriers.

As it relates to other parts of the portfolio, the commercial business in the third quarter, we had some elevated COVID-related costs, particularly in August and September with the Delta variant hitting younger ages more significantly than earlier in the pandemic. So that created some elevated Commercial claim cost pressure in the third quarter. I would note in our Medicare Advantage book, the MCR in the quarter was a little bit favorable to our expectations, which gives us greater confidence here as we head into 2022 on that subset of the overall U.S. Medical book of business. So hopefully, it gives you a little bit of a picture for how 2021 is shaping up.

In terms of your question on looking forward on Commercial utilization, are we caught up, et cetera. We have seen much less deferred care in the Commercial line of business throughout the pandemic and all the indicators that we track, whether that be preventive care utilization or whether that be rates of new cancer diagnosis, et cetera, would tell you that there's not a significant amount of future pent-up demand or catch-up care to come.

With that said, our pricing posture, as David mentioned earlier, continues to be a prioritization of margin expansion as we head into 2022.

Operator

Our next question comes from Mr. Ralph Giacobbe with Citi.

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

I guess I want to go back. You guys specifically called out the increased specialty contributions. And obviously, that's always been part of the story. So hoping you can give more details there, what the specific drivers are there? Anything to call out?

And then maybe within that, I was hoping you could talk about the stop loss product. I would have imagined that just given higher Commercial trend that maybe more of that is being triggered and maybe some underperformance there. But would just like to get your commentary on how that's performed and how we should think about that for 2022 from a price -- repricing perspective?

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

Ralph, it's David. Just a couple of minutes on shaping, I'll hand it over to Brian. As you articulate, the specialty components, so if we look at that broadly back to our strategy, our strategy has been and continues to be how do we wrap the right suite of solutions employer by employer to help to get the overall health and well-being offering aligned and the overall affordability aligned.

And the historic way, one thinks about a specialty suite of a few products of behavioral, pharmacy, dental, has expanded tremendously to 25, 30 different services when you take the subsegments of decision support, chronic care management, specialty services, now virtual alternative services, et cetera.

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So my point of underscoring, this has been, as you articulated and continues to be a really important part of our strategy to try to get the right value to be realized for our clients, our customers and our patients. And as I noted, our Evernorth service capabilities continue to grow, which add to the portfolio of services to be levered there. I'll ask Brian to talk a little bit more in terms of the drivers.

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

Sure, David. Ralph, so in terms of the specialty contributions we called out there, the couple areas I'd particularly point to is more material. Within our self-funded business, we had some strength in pharmacy, in particular. And as I mentioned earlier to a prior question, we would expect that to persist as we head into 2022.

We also saw some upside within our behavioral health offerings as demand for that has continued to grow throughout the pandemic. We saw some increased uptake there, which drove some additional margin for us within the quarter. And again, those are 2 areas we would expect to persist as we head into the new year.

Relative to stop loss, obviously, you've got to pull this one apart further because you got individual stop-loss cover as well as aggregate stop-loss cover and the dynamics there behaved a little bit differently throughout the pandemic, meaning most COVID-related claimants didn't actually hit our individual stop-loss thresholds yet. We saw a little bit of pressure earlier in the pandemic on our aggregate stop loss business. That business gets repriced along with our typical 12-month contract cycles for all the clients that we have. So we feel good about how we're positioned there on a prospective basis.

I'd also note, we're seeing good demand for that product. You probably saw in the supplement there. We had 7% premium growth in our stop-loss line in the quarter-over-quarter. So feeling good about all the specialty solutions when you look at the total portfolio.

Operator

Our next question comes from Mr. Josh Raskin with Nephron Research.

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

So the MLR, I know you guys only disclosed one sort of big MLR for the U.S. Medical segment. So I was wondering if you could break out or give a little bit more color, even if it's just directional on the MLRs for sort of Commercial and then Government and maybe even within Government, how much was from the IFP versus Medicare Advantage?

And then just a quick follow-up on stop loss, what are the attachment points at the individual claim level typically? I know there's a range of those, but kind of maybe what's the most common threshold that an individual as to hit?

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

Josh, I'll try not to be too redundant with some of my prior comments, but just to kind of summarize a few of the important points here as you pull apart the MLR. For the full year, as I mentioned earlier, the refreshed 84% to 84.5% outlook reflects particular pressure from the Individual exchange lives and specifically the Special Enrollment Period in enrollees. So removing that, we would have been toward the higher end of our prior guide of 83% to 84%, but a sub-bullet there is the Individual Open Enrollment lives are actually performing pretty well. So when we look at the profitability of the overall individual portfolio, we have good performance on the standard Open Enrollment lives. We have more performance on the Special Enrollment Period lives and the total picture there is therefore a bit elevated.

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Medicare Advantage, as I made reference to, actually ran a little bit favorable to our expectations in the third quarter. And then Commercial was a touch higher than our projections due to the effect of the Delta variant in the months of August and September, in particular. So those are the broad buckets that I paint for you as you think about what's inside the medical care ratio.

Relative to stop loss, we do have a range of attachment points depending on the clients. So we tend to see particular popularity around $50,000, $75,000 level, but it really depends on the risk appetite for a given client. So it's hard to say that there's one that's always the preferred choice. We have a distribution and the distribution evolves depending on the appetite for clients at any given point in time.

Operator

Our next question comes from Mr. Kevin Caliendo with UBS.

James Kurek - *UBS Investment Bank, Research Division - Associate Analyst*

This is James Kurek on for Kevin. Just maybe with the sale of Chubb, you're signaling more of a focus to core healthcare business. Are there any other segments within the company that you consider non-core that you might be looking to dispose of in the future?

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

It's David. As I noted, the action we took relative to that part of our portfolio and previously, the action we took relative to our Group insurance business we deem to be a good fiduciary management of the portfolio and looking at the strategy as a guide to our actions. Headline is that I would not signal anything of materiality that sits on the horizon. I would reinforce it's a dynamic process, our responsibility is to dynamically manage that, but I would not signal anything on the horizon. And quite proud of the organization and pleased with the successful execution now of both transactions, one, completed; second, under regulatory review right now.

Operator

Our next question comes from Mr. Steven Valiquette with Barclays.

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

So just a question that maybe ties a lot of the other discussion points together. For the preliminary view of '22, I know it's kind of early, but just thinking about the framework of '22 relative to some of your long-term targets that you laid out at the analyst meeting, I'm curious, I mean, so for U.S. Medical, you just talked about growth next year, but the long-term guidance range is 8% to 11% earnings growth in that segment, 4% to 6% for Evernorth and the rest from capital deployment.

But should we think about -- is that still the usable framework going into '22? Or should we think about maybe less operational growth and maybe more from capital deployment? Just any additional thoughts around those components might help, knowing that it's preliminary right now.

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

It's David. The big picture as you look at 2022, I made a brief reference to this previously, but -- our view of the earnings visibility and the growth visibility relative to 2022, essentially, if you take the at least 10%, we underscore that with capital contribution for EPS growth in line with our strategic target, which is 4% to 5%. So then if you back away from that, that leaves you 5% to 6% fundamental organic earnings growth contribution to get to the at least 10% number.

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And we think that's an appropriate and prudent and attractive outlook given the fluid and dynamism of the marketplace. So broadly speaking, both components are in line with our long-term strategic objectives. And we have a track record, including 2021, which is a disruptive year of delivering in line with that. So good fundamentals, a little more than 50% of it being organic, a little less than 50% of it being capital deployment and very much in line with our long-term strategic targets.

Operator

Our next question comes from Mr. Matthew Borsch with BMO Capital Markets.

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

Just wanted to ask what you're seeing in terms of customer preferences and actions in the Middle Market, in particular, the degree of interest in alternate ASO type funding for the products versus what you've seen over the last few years?

And then maybe in the stop loss market that's associated with that. Am I correct that some of the other carriers may be correcting for what was perhaps overly aggressive pricing in earlier years, which is maybe giving you a little bit of a tailwind there on your own growth?

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

Matthew, it's David. So you referenced Middle Market. I don't think there's a singular common definition of Middle Markets. So let me try to frame your important comment. First, as you look at our go-to-market offerings, we have a broad suite of funding alternatives and we seek to offer to our clients their respective decision of how they want to finance their purchase, after the benefits are configured, after the access profile is configured, after the clinical programs are configured and the service models are configured to align, as Brian referenced before, the risk transfer and the balance relative to them.

So having that broad suite is really important. If we look at the Select segment, 100 to 500 life clients, it varies from year-to-year in terms of how much of the client demand is guaranteed costs versus self-funded with stop loss, but self-funded with stop loss has been a meaningful portion. And as you walk from that into the heart of what I might consider Middle Market, the further you walk up in average size on average, more demand for self-funded, less demand for risk transfer and in the -- in between range, some for shared returns of fundamentals that exist.

So a little bit of linearity as you just go up in respective size from that standpoint. But the important part is choice that we offer in the marketplace and try to separate the financing decision from the design features from the program. I would say to the last part of your question, I do not believe that there's a boomerang or a reconfiguration effect that's happened that we benefited from, from a stop loss standpoint. We've seen just consistency in how we use stop loss. And I'd remind you from prior conversations, we have a large book. We have a dedicated team that manages that book because there needs to be specialization in that like many other aspects of our business. And it's both performed for clients, importantly, giving them the peace of mind and revenue predictability and expense predictability they need as well as for us over a long period of time. But I would not call out anything unique in terms of ebbing and flowing that's changed our rate of growth and stop loss over the recent past.

Operator

Our next question comes from Mr. George Hill with Deutsche Bank.

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

David and Brian, just a couple of bean counting ones and a quick question. David, I just want to make sure that $20.35 or whatever the number is post Q4 is the right jumping off point for the 10% or better growth in 2022, given it sounds like you're saying all the other pushes and pulls are mute now.

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Can you quantify PBM to Commercial medical cross sales, the selling season? I'll pause right there.

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

So George, 2 questions I heard. Question one, yes. The at least $20.35 which is our raised EPS is the appropriate jump off to attach to at least 10% growth, and we're pleased to have that underlying strength and that clarity of message.

The second question, I think you're asking relative to PBM Commercial cross-sell penetration, et cetera, respective growth. I don't have an individual number for you. We have not historically walked through individual numbers there. I'd ask you to step back and remember our strategy here. We have a high cross-sell and high integrated offering within our medical business. As you think within the prior question that Matthew asked, as you go to our Select segment, think about that as 100% integrated. It is so integral to our offering.

And as you move upmarket, it's more of a stand-alone sale that needs to be made. We see continued progress there, and we're pleased to either have it as an integrated part of our medical offering or a stand-alone PBM offering that we could harness and sell additional services because at the end of the day, as I called out in my prepared remarks, there are 2 fundamental ways in which a client or a customer establishes their primary health and well-being relationship, either a pharmacy relationship or largely off of a medical relationship and we're positioned to lever both.

So I would leave you with a directional answer on the PBM Commercial. Brian referenced PBM strength or pharmacy strength in our Commercial portfolio. That's a net positive, and we continue to see traction both on stand-alone pharmacy as well as integrated pharmacy within our business.

Operator

Our next question comes from Stephen Baxter with Wells Fargo.

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

Just wanted to come back to the Individual market commentary you made. I appreciate that you're pricing, I guess, conservatively in a fairly competitive backdrop. How much of the way back towards your target margins do you think that's going to get you in 2022? And then how should we think about growth beyond 2022, as you previously have talked about doubling this market through 2025?

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

Stephen, we were seeking to be quite clear in terms of there's -- our view, indisputably, there are some pockets of intense competitive pricing in the IFP marketplace or the Individual exchange marketplace as it's broadly articulated. Given the breadth of our portfolio, we're going to be able to achieve both our aggregate growth as well as our earnings objectives while maintaining price discipline in temporarily dislocated markets, and we deem that to be one.

So we expect to see a net flat or decrement in our volumes in the Individual exchange business and a margin improvement. I'm not going to give you a margin number. We're not guiding in detail for 2022 yet, and we typically don't guide relative to individual margins. Having said that, we expect to improve that margin from 2021 to 2022 to a more attractive and more sustainable level, and we'll maintain the discipline there.

As it relates to intermediate to long term, we continue to see this as a growth market. But as we've managed it and as we demonstrated over time, if there are temporary dislocations, we'll maintain discipline, and we'll lever other parts of the business to ensure the portfolio delivers. And as I noted in my prepared remarks, we've entered 3 more states and almost 100 additional counties to give us access to an addressable market of approximately 1.5 million additional customers to sell to. And we've been in this marketplace since its inception in 2014. And we have a track record of sustained performance, albeit episodically needing to sharpen focus as we will in 2022, given the market conditions.

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Operator

Our next question comes from Dave Windley with Jefferies.

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

David, I'm interested in your views, albeit early on this Build Back Better bill that appears to be moving toward a vote. And maybe specifically, what you think the impact of government negotiation on a top 10 or 20 drugs beyond their exclusivity would have on your PBM business?

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

So clearly, a lot of fluidity right now on the hill, and we've operated for a long period of time in an environment, and we'll continue to, that has an active both legislative and regulatory agenda. So we understand that fully.

Big picture, stepping back, any initiatives that are constructive and sustainable that improve affordability and value for individuals, we're actively open to, engaged in, and generally supportive of. Specifically in the pharmacy space where you double-click down on, we think the most meaningful way that's sustainable policy change that could further affordability is to stimulate and further accelerate more competition. And if I harken back as an example, to make it tangible, hepatitis C was, I think, a very positive example that reinforces that. That is the marketplace rapidly moved from 1 to 2 suppliers for hepatitis C services, which was a breakthrough drug that society benefits from, the overall affordability changed dramatically. That's an action that is different than who's negotiating or it's very different than putting an artificial cap on a rate of growth from that standpoint.

So big picture. We will await the specific details, and we will remain actively engaged, no doubt. We believe the most sustainable way to further improve affordability is to expand choice and expand competition. That's what's worked in the marketplace in the model. And lastly, prior conversation we've had our well-performing and broad portfolio of pharmacy services and tools is well positioned to be able to deliver value in a changing environment, and we're confident and the capabilities we have over the strategic horizon here.

Operator

Our last question comes from Lance Wilkes with Bernstein.

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

Yes. Can you just give a little more color on Evernorth Pharmacy? And what I was particularly interested in is, from a vaccine standpoint in the quarter, how much of that impact volumes and margin? And then are you seeing much impact to margin from specialty pharmacy going generic, whether that's the beginning or your outlook for that?

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

Lance, it's Brian. So within the third quarter in Evernorth, we fulfilled about 4 million COVID vaccine prescriptions. So kind of put that into context, that's about 1% of our total script volume. And year-to-date, we're up to about $16 million across the 3 quarters here in 2021. So again, roughly about 1% of total script volumes for Evernorth, but not a material contribution from an income standpoint. And if that number goes up or down next year, it won't materially move the needle for the Evernorth segment.

More broadly, on the second part of your question, as we think about specialty generics and you can even broaden that to include biosimilars. We're really excited about those for the future from the standpoint of driving affordability on behalf of our clients and customers.

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We think competition is a good thing. And ultimately, specialty generics, while the timing with which they're introduced is hard to predict and does create some variability in our quarterly income patterns, ultimately, we view that as a great thing for our clients, customers and ultimately, for our business. And fortunately, we have a wide range of earnings levers that allow us to capture value in a variety of ways depending on how different client contracts are constructed. So we're really excited about specialty generics and biosimilars going forward.

Operator

I will now turn the call back over to David Cordani for closing remarks.

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

Just to briefly wrap up our call. I do want to underscore how proud and appreciative I am of our more than 70,000 coworkers around the globe who continue to be dedicated to the many stakeholders we serve. Our team is working to support our patients, our clients, our customers, our partners in this very fluid and ongoing challenging environment. And the team has continued to step up time and time again to make sure we're providing the level of support, again, for our clients or customers or patients as well as our communities.

And through it all as an enterprise, we remain focused on executing our strategy, guided by our framework of delivering value every day, partnering and innovating to expand and then expanding our addressable markets to broaden our reach. So we thank you for your engagement today. We look forward to providing future updates on our success going forward and ask you to enjoy the rest of your day. Thanks.

Operator

Ladies and gentlemen, this concludes Cigna's third quarter 2021 results review. Cigna Investor Relations will be available to respond to additional questions shortly. (Operator Instructions)

Thank you for participating. We will now disconnect.

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