THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

ANTM - Anthem Inc at Credit Suisse Healthcare Conference

EVENT DATE/TIME: NOVEMBER 07, 2017 / 6:30PM GMT

CORPORATE PARTICIPANTS

Brian T. Griffin *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

John E. Gallina *Anthem, Inc. - CFO and EVP*

CONFERENCE CALL PARTICIPANTS

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

PRESENTATION

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

I'm A.J. Rice, the healthcare services analyst here at Crédit Suisse. We're very happy to have the management team of Anthem with us today. We have John Gallina, Executive Vice President and CFO; and we have Brian Griffin, Executive Vice President and President of the Commercial and Specialty business division.

You guys had a couple of announcements recently. John, did you want to just open with some comments on -- announcement around the management transition and just sort of thoughts post-quarter.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

Right. Thank you, A.J. Yes, we did. So on Monday morning, we issued a press release and an 8-K announcing a new CEO for Anthem. So just to level set, Joe Swedish is stepping down. He is 66 years old. He's been with the company almost 5 years. He was brought in 5 years ago. The company was a little bit different shape than it is now. When he started, the stock price was below 60. The P/E multiple was just over 9. And in that time frame, we've grown revenues by almost 40%. We've crossed the 40 million member mark in terms of membership and now have over 40 million medical members. Our stock price going into today was over $216 a share, and that stock price appreciation all occurred while we paid an industry-leading dividend for the past 5 years as well. So Joe has also provided a structure for our strategic planning and we now have our strategic initiatives that we're executing on and a really good, solid long-term growth plan.

But we're extremely excited to have Gail Boudreaux join us. Gail is a seasoned executive. I know many of you know her. She knows the health insurance industry extremely well, has really an excellent track record and a very successful career thus far, and we're looking very forward to having Gail start and continue to add value and grow the company.

So that's the management transition. In terms of the company and the business itself, we did also just have our third quarter earnings call few weeks ago. Had a really very solid third quarter financial result. We raised guidance by about $0.25 at the midpoint of the range. Our new guidance is -- earnings per share of $11.90 to $12 per share for 2017; had a declining medical loss ratio, so certainly a very high quality of earnings as well. And we feel we're very well positioned for 2018 with the good foundation that we have. In 2018, we've discussed the fact that we believe -- that we continue to target the, really, the midpoint of our long-term growth projections, our long-term growth aspirations associated with our earnings per share growth. And that -- of course, that's prior to the HIF fee coming back in. The HIF is a headwind that we have to manage around and that will be tracked from our earnings per share growth in 2018 but we're entering 2018 with a very strong foundation.

QUESTIONS AND ANSWERS

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

That's great. And I will say at this point, we're doing -- this is a fireside chat. If people have a question that they wanted to ask, we'll give you a chance to raise your hand and ask it yourself. But if you want to text -- e-mail it to me, I will try to ask it on your behalf.

I'm going to -- surely, there's a lot we can ask Brian about the pharmacy PBM standup. But maybe John, just on the positive medical cost trend dynamic. A lot of the companies are seeing that this year. It seems like, if anything, it might even be a little bit of a pickup versus what we had the last couple of years in terms of favorable trends relative to expectations. Is there anything you'd point to? I mean, I know great management is a key part of it, but anything that's going on? And dynamically, the providers are generally talking about softness. But do you think the increment is the high-deductible health plans? Is it well, -- I'll throw it up on you, and Brian, chime in, too. What do you think is going on in the marketplace?

John E. Gallina - *Anthem, Inc. - CFO and EVP*

Yes. Sure, A.J. Thank you. I would say it's a combination of all those things. It clearly is a very strong medical management and we have excellent clinical programs that we've implemented. Our provider collaboration has really helped ensuring that we have aligned incentives with our provider group, value payment -- or value-based payment systems. High-deductible health plans, clearly, are a part of it. It's a lot of things. We've -- for our health care trend here in '17, we talked about being at the low end of the range that we provided. So we feel very good about that, and there's just -- it's just better control. The pharmacy space that Brian can certainly talk a lot more about has really been a significant contributor to the increase in trend a few years ago. Like for instance, the increase in hep C caused the overall cost trend of the entire medical cost to go up. Well, hep C is more controlled now in terms of year-over-year spending, and so the level of the increases aren't there. It's still a very expensive drug therapy, but the level of increase is no longer as significant as it once was, and so the overall trend then has moderated. Brian?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

No, I think John got it. I think A.J., I'd have to agree. I think the team, the local team's executing in each one of our markets and their focus on medical management. We've really doubled down on our medical management overall, and obviously, to John's point, that we had a significant impact this past year. So that was really critical. And we've really expanded our provider collaboration. It's beyond where we were just a couple of years ago. So now, we're really nationally across our entire enterprise footprint. We've got really solid value-based contracts. I've mentioned in some of the previous discussions, that creates a really nice opportunity for us as we think about pharmacy. And including pharmacy within those value-based arrangements, where typically there's some level of risk involved at the -- between us and the provider, I think that's a nice opportunity for us. And actually moving forward, as we move into the new relationship with CVS Health, we have the opportunity to leverage the provider relationships as well as the pharmacy relationships around and get aligned incentives. So I think that, that's going to create a new opportunity for us to manage both medical and pharmacy trend.

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

Okay. Clearly, as well as the management succession, the announcement of standing up to PBM and the decision to do that in 2020 and '20 beyond. When you think about milestones that you need to do from here and building blocks to get to that point, what are some of the key things that need to be done? What have you already sort of even started to preposition today? I think your outgoing vendor said earlier that your timeframe looks pretty tight. Maybe any comments you have on that in terms of making the transition.

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Sure. Yes. So you may have -- first of all, we're obviously really excited about this launch of IngenioRx. We are -- we're going to be moving forward with CVS Health starting 1/1/20. And to A.J.'s point around the implementation timeline, we've outlined that we're expecting to have that complete migration executed from 1/1/20 through 1/1/21, and we're confident that we'll be able to achieve that. We've got -- we've already started, actually, the implementation planning process of in terms of how do you get there, what are the milestones. We started some of pre-implementation planning. Our team has been doing this on our side for, candidly, about a year, anticipating the conversion of our business. And now, we're getting into deep implementation planning with CVS Health. And so over the next -- between now and 1/1/20, we believe that we've got significant time really to get this planning done right to execute this the right way. Naturally, our key objective in all of this is to ensure that we have no client level abrasion, provider level, or most importantly, member level abrasion as we go through this transition process. But again, we're confident that we can get it done within that timeframe.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

And just to be clear, it's -- really, it's greater than 3 years from the start of transition planning until January 1, 2021, so we feel very comfortable with the 3-year runway. And as Brian said, ensuring that there's minimal member disruption along the way. So just as a reminder, back in 2008, when Anthem, and it was WellPoint at the time, entered into the 10-year contract with Express Scripts, that transition took about a year of planning and 9 months of implementation. So it was less than 2 years before a similar number of PBM members was completely converted from a NextRx platform to ESI platform. So it's not like it hasn't been done before. We did it.

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

Okay. And you've said, in thinking about this, is you think you've got $4 billion of run rate savings. About 20% of that, you see falling through to shareholders right away, but there's a lot of the discussion how it enhances your offering going forward and what that opportunity might present. I'd love you to expand on that a little bit. But also, when you start thinking about pricing the business, whether it's the commercial business, the Medicare, Medicaid, do you have to wait until you actually see those? Can you start incorporating some of that into enhanced competitive contracting early?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes. So maybe I'll tackle that one and John could add some color to it. So to A.J.'s point, we're looking at $4 billion -- greater than $4 billion in savings on an annualized basis, so on a run-rate basis. And then the idea of retaining in excess of 20% of that number. That's purely the CVS pricing versus the in-force contract pricing. So that's really just the unit cost differential. What is not included in that, which we have spent some time talking about, are the areas for growth. So obviously, to the degree that we now have very competitive pricing, really market-leading pricing, we are in a position to grow our core business for sure. Obviously, we've been growing that business despite not having market-leading pricing, and I think we'll certainly be in a position to accelerate our core medical plan growth as a result of improved pharmaceutical pricing. The other key areas, a number of new areas of growth for us that IngenioRx kind of unleashes, we're going to be competing nationally. So today, largely, we're competing just in our 14 commercial markets and our government markets. Here, we'll be able to compete nationally and we'll be able to compete on freestanding or stand-alone pharmacy business for the first time. We're going to be very aggressive about getting into that market and expanding our penetration into that market. And we've not been in that market for the last 7 years, so this is a completely new growth opportunity for us. The other -- a couple of key areas of growth. One is we've got a renewed focus in our group [MA] business. We've had some really nice initial successes here in the near term, in getting back into that business aggressively. As you all know, the pharmacy is a very significant component of the group retiree overall spend. So to a degree that we can now bring in more competitive pricing, we're confident we're going to be able to grow at a higher rate within that business. We can enter into the fee-for-service Medicaid business for the first time. Again, this is fee-for-service freestanding pharmacy. So that's a new market for us. And then lastly, we see this as being a really nice opportunity for us to partner with other of our Blue Cross Blue Shield plan partners and potentially be the pharmacy inside those other Blue Cross Blue Shield plans. So in effect, we become the PBM inside and leverage our scale and our purchasing power to benefit those other Blue Cross plans. So those are the areas of new growth that, obviously, are not included within the $4 billion run rate savings that we've referred to. And then A.J., to your question around how do you price for it. So with respect to PBM contracts in the commercial market, typically, there are 3-year contracts. So in our national account business, at this point, actually, we're bidding on 2019 business. So to the degree that you've got a 3-year contract that then bridges from our existing relationship into 2020, 2021, you can obviously price recognizing that you've got that competitive pricing to support your overall offering. So we are applying that strategy. So that's, again, a nice opportunity for us to grow. And I'd say the last comment I would have in terms of growth is we are going to be very differently positioned than a freestanding PBM. So we're going to be going to market with an integrated value proposition. By that, I mean a medical and pharmacy combined value proposition, where we'll be in the position to -- for example, we'll be able to leverage CVS Health's point of care member messaging, so identifying gaps in care at the retail pharmacy setting. We have the ability through our provider contracts; John mentioned value-based contracting at our physician network. We'll be able to leverage integrated data to identify gaps in care, medication adherence issues to our provider partners as well. And I think the idea that we're going to be able to leverage that value proposition as well as our 40% -- roughly 40% market share in our 14 commercial markets, that really puts us in a position to leverage our provider relationships in the context of this integrated value proposition. So I think we're going to be really uniquely positioned to compete with both the freestanding stand-alone PBMs as well as other health plans.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

And A.J., I'll just finish onto the answer in terms of growth and the growth opportunities that this new PBM contract provides us, and maybe some proof points. And a few of you have heard me say this in the past, but in 2015, we grew by 1.4 million medical members. In 2016, we grew by another 1.1 million medical members. And that was while we had a substandard PBM contract where we were overpaying by an excess of $3 billion a year. And we're able to grow because of the fact that we do have a great value proposition associated with our hospital discounts, our provider networks, our customer service, all the other aspects of the value proposition aside from the pricing on the PBM. And so then you can take a better PBM pricing and couple it with these strengths and these value propositions that we already have, and we believe in 2020 and beyond, we're extremely well positioned to have great growth.

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

When you think about working with the other Blues, will your integrated offering work with them? Will they give you access to the medical data, you think, to be able to offer that integrated?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes. So I think they would, A.J. -- I think to the degree that we could potentially help some of the other Blue plans to be able to execute operationally on that value proposition, my guess is that they would take advantage of it. So then you've got a combination of the value of the financials, really significant operating guarantees and be in the position to share with our sister plans that they can have world-class operating performance while having significant financial value, coupled with the ability to execute on that strategy of an integrated value proposition, the way that I just summarized it, I think that, that will resonate really well within the Blue community.

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

And I think on the announcement and then some of the meetings I've heard today, you're talking about there's also aspects to the contract where you can engage the pharmacist and maybe incrementally to what you've done in the past, some of that provider collaborate, which is a hot topic in the marketplace today. Can you maybe expand a little bit on that and how you're going to hopefully have maybe some pharmacist engagement help you at gaps in care and that kind of stuff?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes. Great. So actually, this is one of the things that was attractive about the CVS Health offering, is that they do have the ability to message the retail pharmacists, whether it's a CVS pharmacist or a Walgreens pharmacist, anyone in the network around gaps in care. And gaps in care could be -- again, I'll stick with the medication adherence. So the patient isn't being adherent with their therapy. And to the degree that we can then bring in medical pharmacy, potentially even lab data, into that, we can really expand on the gaps in care that we're identifying on a retail level. And again, similarly, on the provider side, we're able to port that information into the physician practice management system. Then you've really got a very, very different value proposition where you can have an impact on total health care cost. And I would argue that, that's really where we're different than the stand-alone PBMs. The lens with which we evaluate everything is on total health care costs rather than optimizing rebates, for example, in terms of a freestanding or stand-alone PBM lens. That is very different. And everything that we do in terms of how we define the content of our formularies, our clinical programs, it's all from the vantage point of total health management. And being able to go to market and compete with the freestanding PBMs on that basis, again, I think it's going to put us in a very different position. As you know, we have a significant and growing block of business in the large group local market. That tends to be state systems, county systems, municipalities, labor. And then in the national account market, which tend to be the Fortune 500, that value proposition is what they're looking for. They're looking for someone to manage total health care costs rather than just a slice.

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

Okay. About 10 days after you guys announced your deal with CVS and your own decision to go in-house with your PBM, papers carried a speculation on another transaction involving CVS. That comes across to where you say, "Gee, I wish I would've known that when we did our deal?" Or what's the reaction to that? Does that change in any way the way you think about these opportunities?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes. So it definitely changed the way we look at the opportunities, and I'm sure for many of you in the audience as well, you probably heard that rumor out in the market before it hit the Wall Street Journal. We certainly did. So as we were negotiating the agreement with CVS Health, obviously, we were very much aware of that as a market rumor. So with that, we, as part of the negotiating process, negotiated a fair amount of flexibility and optionality in our agreement with CVS. But the bottom line is, again, we've got -- we're assured of having market-leading pricing, market-leading operational performance which are supported by significant financial guarantees from CVS Health, we are confident that we'll have that completely firewalled off from the rest of CVS' business which is critical from a strategic perspective. So we're really confident that, ultimately, we're going to be able to leverage the economics while creating that integrated value proposition that I defined in a way that is going to create a market-leading value proposition. So we're comfortable with it. We were eyes wide open as we were negotiating the agreement. And we're really feeling good about where we landed in that negotiation.

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

You think there's any reason to be concerned that they're biting off a lot, signing a deal with you, signing -- potentially doing something here that they'll just have trouble meeting their obligations, I guess?

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes. So as it relates to the...

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

Service levels and things like that.

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Yes, yes, I know. It's a great question. As it relates to the pharmacy, I think everybody is aware that CVS Health is the PBM for Aetna already. So Aetna already operates on the CVS platform. So I'm not expecting -- with respect to the teams that we've got that are going to be dedicated to the Anthem migration over to CVS, that we'll have any issues with respect to that migration. I should also note that the -- in terms of the operational guarantees that we have in the agreement, we've got very strong assurances around the implementation process. So the transition is covered by those operating guarantees as well. So yes, A.J., we're feeling good about that. And more importantly, I guess as you think about the implications of that combination, we're also feeling very confident in our ability to execute on that integrated value proposition very differently than any other health plan. So as you all know, we've got, on average, about a 40% share in each of our 14 commercial markets, and that gives us, obviously, a voice at the table within the provider community and allows us to really align our incentives with our providers through value-based contracting very differently than anyone else can because of our density and market share within those markets.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

And the point that Brian made, just to make sure everybody was key on, is that we will have some dedicated teams focused on the Anthem account, which means that there's nothing for them to be distracted by.

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

Right. Okay. During the whole process with the potential buying of Cigna, you guys stepped back somewhat from the capital deployment elsewhere coming out of that, your leverage is a little below where it traditionally has been. How do we think about what capital you have available? You've got a couple of little -- not little -- tuck-in M&A deals that I know you're excited about. Is that where we'll see coming forward with you as well as I think you stepped up the buyback gradually over the course of this year as well. Give us some flavor, can't let John off completely here -- give us some flavor for the capital deployment priorities.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

Yes. No. Thank you for the question. I think any good capital deployment strategy is well-balanced between share buyback, dividends, mergers and acquisitions and investing in the business. And I do think we have a good, well-balanced capital plan. Right now, our debt to cap is about 38% and we're targeting to be closer to 40% long term. As a matter of fact, we can access some debt to get up into the low to mid 40s in order if we need it to help fulfill some of our capital needs. And as you said, we have announced 2 acquisitions here over the past month or so, MA plans in Florida, HealthSun and America's 1st Choice, along with the Simply Healthcare acquisition from a couple of years ago, really gives us a good solid presence in Medicare Advantage in Florida, which is a great market to be -- have a good solid presence in. And so we obviously utilized capital for that. The share buyback here in 2017 we talked -- after the Cigna deal, when we walked away from that, we really didn't do any share buyback for over -- well over a year. We talked about $1.5 billion to $2 billion. We're on track to be at the high end of that range for 2017. And that was really only starting in April. I think we have had about 1.6 billion of buyback through September 30. So I would expect that a $1.5 billion to $2 billion normalized share buyback for the next few years as part of our long-term growth trajectory. Again, we pay one of the highest dividends in the marketplace, and we reevaluate our dividend every year with our board, but there's no reason to believe that it will look any different than what it has in terms of being at the high end of the industry. And then reinvesting in the business. We're making some investments here in 2017, and we will, in 2018, continue to position ourselves for future growth. So I feel very good about our balance of capital deployment and I'm really targeting to get down to closer to 40% debt to cap on a long-term basis.

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

And when you think about acquisition opportunities, you said 2 that are sort of MA-focused? But is that where the focus will be? Or is there capabilities, other things that are on the priority list in terms of things you might look at?

John E. Gallina - *Anthem, Inc. - CFO and EVP*

That's a great question, and opportunistic is the word that I think really comes to mind in terms of where we'd head on a merger and acquisition-type basis. As I said, during this Cigna transaction, or at least trying to complete the Cigna transaction, we didn't really look at a lot of these opportunities. And then once we walked away from that, there are several that we looked at. And the tuck-in acquisitions and MA being a high-revenue, high-growth area, really, a geography that really helped solidify it, that was our immediate priority. But there are -- we'll continue to look at tuck-in acquisitions and our other lines of business that are very desirable as well, and capabilities that are very desirable as well. We don't want to limit ourselves to any of them, but I think we'll continue to look at several and be opportunistic on whichever ones that we decide to execute on.

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

I'll just ask a question if anyone had a question they want to asked in the audience, feel free to do so. You've got a couple of -- I don't know if there's anything to be said here but I'm going to ask it. Pending litigations, both the debate over the breakup fee with Cigna, but also with your current PBM vendor, any updates on either one of those? And...

THOMSON REUTERS

John E. Gallina - *Anthem, Inc. - CFO and EVP*

No significant updates. There's still discovery ongoing. No trial date has been set yet for the Cigna breakup fee. The Express Scripts, we're going through the discovery on that and I believe we expect to go to trial sometime in 2018. We feel very good about our position in both; very good.

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

Is there anything, capital deployment, strategically, otherwise, that you're waiting for those to play out that's holding it up? Or is it business as usual pretty much regardless of what happens with those?

John E. Gallina - *Anthem, Inc. - CFO and EVP*

It's business as usual. I said we feel very good about our position. On the Express Scripts, it's only upside, so obviously, that wouldn't preclude anything. We are very cognizant of the issues associated with the Cigna litigation, but feel very comfortable with our position, and that would not preclude us from looking at another opportunistic M&A opportunity.

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

Okay. Well, that's great. I appreciate Anthem participating in our conference. They are going to do a breakout session. That will be in Room 1. And we have a break in this room next. So thanks, everyone.

Brian T. Griffin - *Anthem, Inc. - EVP and President of Commercial & Specialty Business Division*

Thanks, A.J.

John E. Gallina - *Anthem, Inc. - CFO and EVP*

Thank you.
