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Anthem, Inc. (ANTM) CEO Gail Boudreaux on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-23-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $4.87 beats by $0.05 | Revenue of $26.44B (15.07% Y/Y) beats by $566.94M

Earning Call Audio

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Anthem, Inc. (NYSE:ANTM) Q3 2019 Results Conference Call October 23, 2019 9:00 AM ET

Company Participants

Chris Rigg - Vice President of Investor Relations

Gail Boudreaux - President and CEO

John Gallina - CFO

Pete Haytaian - President Commercial and Specialty Business Division

Felicia Norwood - President Government Business Division

Conference Call Participants

Ralph Giacobbe - Citi

Justin Lake - Wolfe Research

A. J. Rice - Credit Suisse

Ricky Goldwasser - Morgan Stanley

Kevin Fischbeck - Bank of America

Steve Tanal - Goldman Sachs

Matt Borsch - BMO Capital Markets

Peter Costa - Wells Fargo

Gary Taylor - JP Morgan

Steven Valiquette - Barclays Capital

Lance Wilkes - Bernstein

George Hill - Deutsche Bank

Josh Raskin - Nephron Research

Scott Fidel - Stephens

Dave Windley - Jefferies

Sarah James - Piper Jaffray

Michael Newshel - Evercore ISI

Charles Rhyee - Cowen

Operator

Ladies and gentlemen, thank you for standing by and welcome Anthem Third Quarter Results Conference Call. At this time, all lines are in a listen-only mode. Later, there will be a question-and-answer session. Instructions will be given at that time [Operator Instructions]. As a reminder, this conference is being recorded.

I would now like to turn the conference over to the company's management.

Chris Rigg

Good morning. And welcome to Anthem's third quarter 2019 earnings call. This is Chris Rigg, Vice President of Investor Relations. With us this morning are Gail Boudreaux, President and CEO; John Gallina, our CFO; Pete Haytaian, President of our Commercial and Specialty Business Division; and Felicia Norwood, President of our Government Business Division.

Gail will begin the call by giving an overview of our third quarter financial results, followed by comments on our key business initiatives and enterprise-wide growth priorities. John will then discuss our key financial metrics in greater detail, and go over our updated 2019 outlook. We will then be available for Q&A.

During the call, we will reference certain non-GAAP measures. Reconciliations of these non-GAAP measures to the most directly comparable GAAP measures are available on our Web site, antheminc.com.

We will also be making some forward-looking statements on this call. Listeners are cautioned that these statements are subject to certain risks and uncertainties, many of which are difficult to predict and generally beyond the control of Anthem. These risks and uncertainties can cause actual results to differ materially from our current expectations. We advise listeners to carefully review the risk factors discussed in today's press release and our quarterly filings with the SEC.

I will now turn the call over to Gail.

Gail Boudreaux

Thank you, Chris and good morning. Today we reported third quarter 2019 GAAP earnings per share of $4.55 and adjusted earnings per share of $4.87, reflecting strong revenue and earnings growth across our businesses.

Operating margin was 5.8% for the quarter, a substantial improvement, both sequentially and year-over-year. Over the last several quarters, our enterprise-wide financial results have been strong and in 2019, we will exceed our long-term revenue and earnings growth targets. Anthem's third quarter operating revenue increased a robust 15% over the prior year quarter to $26.4 billion. Medical membership across all of our businesses increasing by 1.1 million consumers served with our risk businesses accounting for nearly 90% of total growth.

Anthem Specialty businesses also delivered solid growth, adding nearly 150,000 new consumers in the quarter and nearly 800,000 to the first months of this year, first nine months. Anthem Full Health Connection has been a key enabler of our strategy to increase specialty product sale, by integrating information across our packaged medical and specialty offering, driving more effective innovations to close gaps in care and reduce costs.

As part of Anthem Whole Health connection, we identified that dentist account for nearly 10% of opioid prescriptions. By leveraging this insight and mobilizing our local provider network and clinical teams, we initiated a multiyear effort to broadly educate Anthem dentist on effective non-narcotic alternative. As a result, opioids prescribed by our dental providers decreased by more than 50% and the number of opioid prescriptions exceeding 7 day supply were cut by more than 90%.

Our clinical focus is designed to support care providers by giving them data, tools and capabilities to effectively manage performance. This example illustrates the power of our focus on whole person health to deliver improved outcomes and reduced costs, while impacting one of the most pressing healthcare issues facing society today.

The migration of our pharmacy business to IngenioRx continues to go extremely well, and we remain on track to have all of our members on the IngenioRx platform by January 1, 2020. We're confident in our ability to execute on the remaining aspects of the transition, and now expect to be in a position to provide value added services at much more competitive pricing. IngenioRx is a key example of the strategic end-to-end execution that we're driving across all aspects of our business.

With each successful wave of our migration, we've implemented a command center model bringing together hundreds of associates, representing critical operational areas to work side-by-side 24/7. Through this model, we've been able to monitor performance in real time and deploy cross functional [SWAT] teams to quickly and effectively resolve any issues or concerns.

Medicaid results improved this quarter, but at a slower rate than previously anticipated, as we had better alignment of revenue relative to the risk profile of the populations served. We added nearly 200,000 members and see continued strong growth through 2020. We remain confident we'll continue to improve our performance, while delivering even greater value for our state partners and the individuals that we serve in our Medicaid programs.

Our previously announced acquisition of Beacon Health remains on track to close late in the fourth quarter. This strategic addition to the Anthem portfolio will strengthen our market position in behavioral health and help further our efforts around whole person care. Improving performance execution around Anthem remains a key priority and focus. We've made progress in many areas but there is still more work needed in order to unlock the full potential of our enterprise.

We're very disappointed with the recently announced star rating scores for payment year 2021, which did not improve at the rate we had targeted. Unfortunately, these ratings were largely impacted by our Clinical Pharmacy results. However, with the successful transition to IngenioRx, we have refocused our organization with clear accountability and line of sight to deliver dramatically improved results going forward. We are absolutely committed to improving the percentage of our members in four star plans.

Across the Anthem, we remain intensely focused on creating innovative, meaningful and affordable products and services for our customers, consumers and care provider partners. We continue to invest in digital capabilities and AI in order to create the kind of healthcare experience our consumers demand today.

Our recently launched electronic personal health record is gaining traction. This unique tool is empowering consumers to be more engaged in healthcare decisions by supporting greater alignment and communication with their own care providers. We're excited about the launch of Sydney, our next generation consumer engagement platform.

Sydney is delivering on our promise of a simpler, more personalized experience, giving consumers control over where and how they engage with us regarding their care, benefit coverage, their health and wellness goals and more. By leveraging data and AI, Sydney is providing a personalized healthcare experience tailored to each individual's unique needs, resulting and improved engagement and ultimately a lower total cost.

Turning to 2020. In Commercial, we anticipate another solid year of both risk and fee based membership growth. In addition to the benefit of IngenioRx, we've deployed a broad portfolio of innovative products to meet our customers where they are. These include Anthem's recently announced chamber based association product along with the newly launched HealthSync high performing provider network, giving employers more affordable choices.

We anticipate another strong year of national account growth. National account customers represent our most sophisticated buyers and our success is determined by our ability to deliver better quality at the lowest net cost with improved member satisfaction. Clinical programs, such as Total Health Total You, our integrated end-to-end digital-first clinical model, are exceeding expectations on this front. Since launching in January of this year, we've added one million members and expect to have approximately 2 million consumers in 2020.

In Medicare Advantage, we're pleased to have grown enrollments by nearly 20% in 2019, and remain confident that we will continue to outpace the market for the fourth consecutive year, based on the value we deliver to seniors through our highly attractive plan design and supplemental benefits. We also anticipate continued growth in our group retiree business.

For 2020, we're enhancing our supplemental benefit choices, which are highly valued by seniors and include areas such as transportation, caregiver support and nutritional education, to name just a few. These services are an addition to our already successful over the counter benefit in partnership with Walmart. Our efforts in this area are proving that Anthem's unique focus on whole person care is truly resonating with this important population.

As you know, our Medicaid business is well positioned for robust membership and revenue growth in the year ahead. Our partnership in North Carolina is expected to go live in the first quarter, and will add approximately 400,000 members. Supplementing our strong organic growth, we look forward to working with our state partners to serve members in Missouri and Nebraska upon completion of the Centene WellCare transaction.

Our commitment to sustainability also remains a key focus for our organization. With that, I'm pleased to share that Anthem was named to the Dow Jones Sustainability Index for the second year in a row during this quarter. This recognition acknowledges our commitment to responsibly address the challenges facing today's dynamic and ever evolving healthcare environment.

At Anthem, our focus on culture and talent continues to serve as our foundation for success. We are enhancing talent across the organization to support our focus on growth and improve our performance execution. We're not satisfied and know we can and will do more to improve Anthem's impact across the healthcare system for those we serve.

I will now pass the call over to John for a more detailed review of our third quarter financial performance before concluding our prepared remarks with our initial assessment of 2020. John?

John Gallina

Thank you, Gail and good morning. As Gail stated, we reported solid third quarter financial results with adjusted earnings per share increasing 28% year-over-year to $4.87. Adjusted net income was $1.3 billion in the quarter, up 25% over the prior year. In total, our consolidated operating gain grew by more than 22% over the prior year quarter.

During the second quarter we shared with our outlook for improved segment performance in the second half of the year. The government business grew operating gain by 35% in the quarter, while the commercial business grew by more 11% compared to the third quarter of 2018. As you can see, not only that we deliver on our commitments, we generated substantial double-digit growth in doing so.

Operating revenue in the third quarter of 2019 was $26.4 billion, an increase of 15% versus the prior year quarter and 17% on a HIF-adjusted basis. With our updated outlook, we now expect full year operating revenue of approximately $103 billion with premium revenue now in the range of $94 billion to $95 billion. We are firmly on track to deliver our strongest year of organic operating revenue growth in over a decade.

The increase in operating revenue during the quarter reflects strong enrollment growth in our risk-based businesses, as well as premium increases to cover overall cost trends. In addition, our results benefitted from revenue related to the launch of IngenioRx and the growth in our specialty and integrated clinical offerings.

The medical loss ratio in the third quarter was 87.2%, representing an increase of 240 basis points over the prior year quarter. The increase was predominantly driven by the one year waver of the health insurer fee. In the quarter, reserves developed somewhat unfavorably, including favorable prior year development and unfavorable current your development. The unfavorable development totaled $50 million and was isolated to the commercial segment. This included a few large groups that we'll be terminating later this year. The magnitude of the impact is immaterial, representing only 0.5% of our full year benefit expense, but it did impact the medical loss ratio in the quarter.

Overall, third quarter medical costs were well contained, and our local group medical costs trend is reaffirmed at our 6% plus or minus 50 basis points range. It is important to note that the Medicaid MLR improved on a sequential in year-over-year HIF-adjusted basis despite ongoing disenrollment. We continue to expect further margin stabilization. But given the magnitude of the Medicaid re-verification challenge we faced in 2019, our full year MLR is trending in the range of 86.5% to 86.8%.

Our SG&A ratio was 12.9%, a decrease of 250 basis points compared to the prior quarter. The decrease reflects our historically strong top line growth, coupled with a one year waiver of the health insurer fee. For the full year, we now expect our SG&A ratio to be in the range of 13% to 13.3%.

Turning to the balance sheet. Our debt-to-cap ratio was 40% at the end of the third quarter, which is consistent with our target range. During the third quarter, we successfully completed a debt offering to $2.5 billion at a weighted average coupon of 2.98% and a weighted average life of 15 years. I am especially pleased that our 10 and 30 year notes were issued at all time record lows.

Efficient capital deployment and cost discipline remain top priority. Earlier this year at our Investor Day conference, we committed to an opportunistic capital deployment strategy focused on sustainable long term total shareholder return. So far this year, we have announced plans for two strategic acquisitions. One of which expands our footprint in Medicaid, while the other deepens our clinical expertise and managing specialized populations. Simply put, we're building our business and investing strategically.

We also committed to a capital deployment plan that would be both flexible and balanced. After careful consideration of the market environment, we made the decision to accelerate our pace of share repurchases in the quarter, and take advantage of the broader market conditions. As a result, we repurchased 2.4 million shares during the third quarter at a weighted average price of $266.52, and we now expect the 2018 share count to be in the range of 260 million to 261 million shares. Total share buyback for the year is expected to be between $1.6 billion and $1.8 billion subject to market conditions.

Operating cash flow was $1.7 billion in the quarter or 1.4 times net income, signifying high earnings quality for the quarter and representing an increase of $1.1 billion compared to the third quarter of 2018. The increase was primarily driven by membership growth in our Medicaid and Medicare businesses. For the first nine months of the year, operating cash flow was $4.7 billion or a solid 1.2 times net income. As a result of our strong growth year-to-date and proactive efforts to better manage our cash and the timing of collections, we now expect operating cash flow for the full year to be greater than $5.5 billion.

2019 has been a productive year at Anthem. Despite the challenges we faced early on, we have made substantial progress, including the launch of IngenioRx, which is now expected to contribute at least $1 to full year adjusted earnings per share. As a result, we're raising our full year guidance and now expect our 2019 adjusted earnings per share to be greater than $19.40. We are fully committed to driving the lowest net cost of care for our members, while achieving greater diversification across our businesses. Both of which are reflected in our double digit top and bottom line growth targets. There is still one quarter left in 2019 and our focus is on driving sustainable long-term value and completing 2019 on our growth trajectory, enabling us to enter 2020 with positive momentum.

And with that, I will now pass the call back over to Gail.

Gail Boudreaux

Thanks, John. As you've heard throughout this morning, we are growing on all fronts. Our revenue growth is strong and we have made substantial progress in advancing our mission of driving higher quality care at the lowest net cost.

As we begin to shift our focus to 2020, the headwinds that we faced are manageable with tailwinds that lay the foundation for compelling long-term growth, and far outweigh the impact from short term challenges. Our growth heading into 2020 is fueled by our commitment to precision and execution with an emphasis on sustainable value for our stakeholders.

As is customary, we will provide more detailed outlook for 2020 on our fourth quarter earnings call, but our initial view of 2020 contemplates the following tailwinds; the full year impact from IngenioRx, margin improvement in Medicaid, overall 2019 and 2020 membership growth, increased penetration of specialty and clinical programs in our fee based businesses and accretion from capital deployment. These will be partially offset by margin normalization in the individual business, dilution from government contracts in Medicaid and growth in our group Medicare and the return of the health insurance fee.

At this early stage, our view on 2020 would point to core adjusted earnings per share growth near the low end of our 12% to 15% target growth rate relative to our original 2019 guidance. We continue to expect IngenioRx will produce total operating gain of at least $800 million, or roughly $2.30 per share in 2020. We're on track for another year of historically strong revenue and earnings growth, and we look forward to building on our momentum in the year ahead. As I approach my second anniversary here at Anthem, I mean incredibly proud of them more than 60,000 associates who are living our mission, vision and values every day in service to those who trust us with their care.

And with that, operator, we will open it up to questions.

Question-and-Answer Session

Operator

Ladies and gentlemen, we will now begin the question-and-answer session [Operator Instructions]. Your first question comes from the line of Ralph Giacobbe from Citi. Please go ahead.

Ralph Giacobbe

Just hoping you could start with providing a little more details on the unfavorable reserve development within commercial. And I know you quantified the impact in the quarter. How much of that sort of fee reflects the higher MLR outlook for the year as well and any details around that? Thanks.

Gail Boudreaux

Thanks, Ralph. I'm going to ask Pete Haytaian to talk about our commercial business, which we feel very strongly about and then maybe John to tie up the overall MLR question.

Pete Haytaian

As it relates to our Commercial fully insured business, earlier this year, we set out to do a couple things. Number one, to grow our membership and we want to improve our year-over-year operating performance. And I'd say with confidence that we've done both. Our year-over-year operating margins and performance has shown strong improvement. And you can see that through the release. In addition to that, we've seen solid membership growth. In fact, in our large group fully insured business, we've seen in nine of the last 12 months net sequential growth, so we feel really good about that.

The in-year unfavorable development is really immaterial. We had a few large groups and being a blue. We have some large fully insured groups but we didn't have a meeting of the minds with, quite frankly. And so those groups are going to be moving on. And as it relates to our outlook Q4 and into 2020, we feel very comfortable with our fully insured business.

John Gallina

And Ralph, this is John, thank you for the question. And I really appreciate the opportunity to provide a little bit of clarity. To be clear, Medicaid and more specifically the Medicaid verification process, is driving the entire increase in the increasing MLR guidance. And I'll just give you a couple proof points if you'd like them for your modeling and your information. In some states, re-verification efforts have minimal impact. But in others, we've seen disenrollment on the average of 2% with states going as high as 4% disenrollment. In those same states, if you review the statutory filings from the first six months of the year for us and our peers, you'll see that the MLRs associated with those remaining populations are up on average 3% year-over-year with some states being up as high as 5% year-over-year.

And as we have told you in the prior quarter call, the re-verification has impacted a little over half of our states at this point in time. And if you just take that 3% times half our Medicaid block and apply it to our consolidated medical loss ratio, you'll see that the consolidated medical loss ratio will go up 50 basis points.

And then just another quick proof point for your modeling purposes is we've made commentary that we're at the low end of our target margin ranges associated with Medicaid for the year associated with the lack of revenue on the re-verification, the time with the lack of revenue on re-verification. And the difference between the midpoint of our operating margin and the low end of our operating margin, if you apply those dollars again to the medical loss ratio, you'll see that it would drive the consolidated medical loss ratio by about 50 basis points.

So both of these things are just proof points to show that the entire increase is associated with Medicaid and that the commercial issue, which was only 0.5% of annual benefit expense really didn't drive that guidance change. So thank you for the question.

Operator

Your next question comes from the line of Justin Lake from Wolfe Research. Please go ahead.

Justin Lake

Just one numbers question here, and then I'll ask my actual. Obviously, a lot of focus on 2020. Just want to make sure I got the math right here. We start with around $18.20 of core EPS, that's the guide of $19 minus Ingenio coming into the year. And then add 12% to that and grow that by 12% gets us in the low 20s. And then we add back the entire Ingenio of $22.30, and you get somewhere between $22.50 and $22.60. So I know the range is going to be wider than that. But is that about the right math?

Gail Boudreaux

In terms of -- we're not giving exact guidance. As you know, we're giving headwinds and tailwinds. But as you think about your math, I'd say you're in the ballpark clearly to what we articulated at our Investor Day this past spring, so yes.

Justin Lake

And then my question was just a follow up on Medicaid. Specifically, I know you said things got better. So in the first half, you were running at the low end of your range, so let's say 2%. Can you give us an idea of what you are expecting to do in the back half of the year in Medicaid, back half of this year? And then how we should think about Medicaid into next year. What's in that 2020 number for a Medicaid margin just so we can kind of have a have a starting point. Thanks.

John Gallina

The low end of the target margin range for Medicaid is where we actually expect us to be relatively close to for the entire year. But the second half is definitely going to be better than the first half in terms of 2019. And then in terms of 2020, we do expect ultimately to be in the target margin range associated with Medicaid. Unfortunately, the timing doesn't always work out perfectly and sometimes it can take 12 to 18 months to get the appropriate rates associated with our negotiations and sharing of information with our state partners.

And so we clearly have expectation of improvement associated with Medicaid in 2020. But it's really premature to provide an exact percentage, or where we are exactly in the range at this point until we get to the point that we'll provide a lot more guidance metrics on the fourth quarter call.

Gail Boudreaux

And let me just add to John's comments. I think, overall, in terms of Medicaid, we feel quite good about the conversations we're having. As he shared with you in terms of the re-verification and the data that we have, we're working very proactively with our states. And again, a lot of this comes down to timing and their cycles. But we feel quite good about what we've been able to achieve to date and also what we feel for 2020. So we're very positive about the overall Medicaid environment business going forward. Next question, please?

Operator

Your next question comes from the line of A.J. Rice from Credit Suisse. Please go ahead.

A.J. Rice

Just maybe to continue to trying to think about the 2020, what's in what's not. It sounds like you guys were assuming again the public exchange business normalizes margin. I know you had an assumption of a declining margin for three years in a row and continue to outperform it. Is that just conservatives or do you know something that would suggest that that's going to moderate? And then in Ingenio, it sounds like you're assuming that you got the same upside that you had originally forecast in terms of gain. It sounds like things have gone at least as well if not a little better. Is there any chance of upside there? And then finally, the Medicaid just to follow-on on that question, are you -- when you talk about what’s the margin for next year and what's assumed in that number. Is that only what you have realized so far in terms of true ups, or are there more true ups that are potentially on the table that you haven't yet realized that would be potential upside?

Gail Boudreaux

So thanks for the multitude and multi-faceted question, A. J., I think you hit most of our businesses. So let me start with John and have him address the first part of it and we'll see if we can get through it. Thank you.

John Gallina

So yes, we do expect normalization of individual margins in 2020. And just as a frame of reference, in 2016 and 2017, we performed essentially at a breakeven basis in that line of business. We never really lost money on the exchanges but it was essentially breakeven. And then we reduced our footprint quite dramatically in 2018 by some 65% and walked away from almost a million members and had extremely successful 2018, and are having a very good 2019. We expect the margins to moderate in 2019 and they have, but not quite as quickly as we had assumed.

And then you get into 2020, while the way that the MLR rebate rules work is it's based on a three year rolling average. And so the 2017, and '18, '19 rebates would have had the prior information in them with when we were much larger. And then you get to 2020 and we've got three fairly good years assuming that we hit our target margin ranges for 2020. And so that’s going to actually limit the ability to have incremental upside.

Gail Boudreaux

In terms of IngenioRx, first of all, we were really pleased with the way the transition has gone and the migration of our members. As you saw, we up our guidance and that's really a result of both strong operational execution, but also greater certainty now when we first gave it. We didn't know exactly when our state approvals would occur in Medicaid and commercial and now obviously, that we have certainty on.

And again as I shared in my opening remarks really strong execution of the migration, probably one of the most complex migrations that has happened in the space, so we're really pleased about that. And we feel very good going into 2020 that all of our businesses will now be on that platform. And we can use our integrated capabilities and the digital things that we advanced over the last year. So thank you very much for the question. And next question, please.

Operator

Your next question comes from the line of Ricky Goldwasser from Morgan Stanley. Please go ahead.

Ricky Goldwasser

A couple of questions here, so just first a follow up on the unfavorable reserve development that you saw in the commercial business, I understand that that's immaterial to the bottom line and not going to have an impact in the fourth quarter. But can you talk little bit about what you're seeing in terms of the competitive marketplace and how competitors are responding to the fact that you now have just better economics and ability to provide more affordable offerings? So that is question one. And second of all, if you can give us any early read now that the Medicare for 2020 plans are out there, how do you see the landscape and opportunities compared to before and anything that surprised you?

Gail Boudreaux

We are going to try to limit to one question. I know we're getting multiple, but we'd ask that we would just wanted to one question. And let me ask, Pete, first to comment on the commercial marketplace competitive.

Pete Haytaian

Yes, I think as it relates to our fully insured business, it remains a competitive marketplace, it remains a rational marketplace. We're real excited about our positioning. We've talked before about our segment positioning and our product portfolio, and the options that we're creating in the marketplace. And we are seeing an uptick there in terms of performance. And we continue to see growth, as I mentioned before, nine out of the last 12 months, we've seen net positive growth.

One thing that we are seeing in the marketplace today and that is with the addition of Ingenio and other capabilities that we have. We are seeing in other markets have a bit of inertia little bit more than we expected. And what I mean by that is retention rates are really, really strong for us and for our competitors. Our sales close ratios are improving, and that has to do with our sales effectiveness, and we feel really good about all that. But we are seeing a little bit less movement in the marketplace, a little bit more stickiness with the membership. And so little bit slower rates of uptake. But other than that, we feel really good about our positioning in the fully insured marketplace going into 2020.

Gail Boudreaux

And I guess what I would just add to Pete's comments. I mean, we've had really solid growth. We think it's a disciplined market. It's always been competitive. We were very happy with the solid retention rates we're seeing. And we've invested quite heavily in that business, both in product offerings. So we feel well positioned for 2020 with a variety of affordable options, particularly in our small business area.

And as I shared, we're seeing great traction in our largest clients who are really our most sophisticated and are really valuing the innovation that we brought to the market. So overall, as Pete said, it's a very, very -- we feel very strongly about the commercial business right now. And maybe Felicia Norwood can address the Medicare question you had as well.

Felicia Norwood

Sure Gail, thank you. And Ricky, thank you for the question. We feel very good about our positioning in terms of our portfolio on the Medicare side as we head into AEP. As you know, we're about what day nine into this, but the feedback has been incredibly positive from our distribution channel and our brokers. In 2019, as you know, we were one of the first plans carriers to really make a strong investment and supplemental benefits.

We believe that these are some of the most differentiating characteristics in the market with respect to our seniors. And we've seen great receptivity to the benefits that we have out there. This is particularly true with respect to our over the counter benefits with Walmart, which has brought great cost advantage and affordability to seniors. So as we head out into AEP, the competitive positioning is strong. We've enhanced our supplemental benefits offering this year as well. So we are very bullish about our expectations with respect to the 2020 selling season in Medicare.

Operator

Your next question comes from the line of Kevin Fischbeck from Bank of America. Please go ahead.

Kevin Fischbck

Maybe just following up on that Ingenio and the Commercial market, but maybe a broader question across all of the products, with the savings that you got for 2020. How much of that benefit did you flow through immediately into 2020? Just trying to get a sense of, was 2020 your fully updated view on pharmacy costs, and the growth that you guys or will get in 2020 is kind of reflective of what that new base is or did you -- because of the transition or for whatever reason you kind of slowly build that into the pricing so that we should expect a multiyear benefit from your membership? And did you treat Medicare or Medicaid -- or Commercial any differently, as you thought about pricing and that benefit through to the customers and the pace of that timing?

John Gallina

Sure. Thanks, Kevin. This is John. And if I understand your question properly, the benefit in 2020 is we know that the value that we're obtaining from Ingenio is approximately $4 billion, actually slightly greater than $4 billion versus what we have would have paid on with our prior carrier. And that we're going to take 20% of that and drop to the bottom line, which is the $800 million that was part of Gail's prepared comments, which is $2.30 of EPS. And then the $3.2 billion is being baked into either benefit design or more affordable pricing, or other options that flow straight to the customer.

In terms of the timing of all that, we really did not let any of that assumptions go through in 2019. 2019 for the majority of the year, we're still under the ESI contract and the pricing that we have with our book really did represent the pricing of the pharmacy costs that we're employing. So don't over read into or overanalyze the 2019 versus 2020. The Ingenio is providing about $1 in '19 and it's going to provide about $2.30 in benefit in 2020, and that $2.30 is now run rate.

Operator

Your next question comes from the line of Steve Tanal from Goldman Sachs. Please go ahead.

Steve Tanal

I think unfavorable development sort of situation seems like an isolated issue. But it sounds like you wouldn't have had a favorable development on the commercial business, excluding the large group you mentioned. I don't want to put words in your mouth, but that's sort of the message that I feel like we're hearing. And so I guess typically, we'd expect some favorable development. So just looking for any color you could provide and the balance of the business. And is your view of sort of local group trend at this point that has sort of accelerated through the first nine months of the year, realizing you reiterated your outlook. But any color maybe and where you might land in the range? So that could be helpful as well.

John Gallina

In terms of the development, we did have favorable prior development. The development that we referenced was current year in-year we usually don't talk about that. But since it was -- it did impact the MLR slightly and it certainly had impacted the commercial operating gains where Commercial grew 11% quarter-over-quarter, Commercial expanded their margins by three tenth of a percent quarter-over-quarter and that was in spite of this negative development. So really what it points to is the fact that the commercial business is even stronger than it may appear initially. But we did have favorable prior year development. We certainly have a consistent conservative reserving methodology that we will expect to employ.

Gail Boudreaux

I guess, I would add to John's comments that our commercial growth is very solid, and we have very healthy margins. And I think as you look at our margins overall, we feel very good about commercial business. And again, the amount of reserve development is fairly minor but we felt that we would point it out. And I think exactly as Pete addressed that that's really the driver. So we wanted to give you some clarity on that. Next question, please.

Operator

Your next question comes from the line of Matt Borsch from BMO Capital Markets. Please go ahead.

Matt Borsch

I was hoping you could maybe give us a sense of how things look as you're going into January 1 in terms of -- I'm not looking for guidance for the year, just start a sense on the January 1 national account changes and how you think you did it in that process, and whether the very strong retention rates that you referenced earlier. Is that playing out in that market as well?

Gail Boudreaux

I'll let Pete address that question.

Pete Haytaian

We're obviously in the late innings. We're sort of in the ninth inning of the selling season. As it relates to 2020, there's some minor puts and takes but it's almost complete. And we feel very good about our positioning and our results. We had a good year this year. And going into 2020, we think we're going to have a very strong year as well from a growth perspective and a retention perspective. Most importantly, and as Gail pointed out in her prepared remarks, we feel really good about our value proposition and how that's playing out in the marketplace.

Things like our total value story and clinical programs and advocacy programs like Total Health Total You, which we've just recently launched with differentiated AI capabilities and care management capabilities, already have over 1.2 million members in that program. We feel really good about our consumer engagement platform and the work that we've done historically through Engage and now we've launched and rolled out the new Sydney digital platform and ecosystem. And our Anthem Health Guide from an advocacy perspective really, really performing well and resonating in the marketplace with over 8 million members in that with MPS scores that continuing to improve. So our value proposition is playing out in the market. We will have a strong Q1 with respect to growth in our national business.

Operator

Your next question comes from the line of Peter Costa from Wells Fargo. Please go ahead.

Peter Costa

[Technical Difficulty] on the commercial development -- unfavorable development. What exactly caused the unfavorable development? Was it a provider specifically that was higher cost? Was it a product type higher cost? Was it some geography? I'd love to drill down and understand what exactly caused that. I know you said its couple of accounts, but I want to understand more.

John Gallina

That's not the type of information for competitive reasons that we're really going to go into on this call, especially given the fact that those accounts have terminated once we determine what actuarially justified rate increases would be. I'd just say that we understand what the causes were. We priced the forward trend. We feel very comfortable that this issue has been taken care of. And we feel very bullish about our aspects. But we really can't get into the level of granularity for competitive reasons that you're talking about.

Operator

Your next question comes from the line of Gary Taylor from JP Morgan. Please go ahead.

Gary Taylor

I just want to go back to the really strong government operating income growth, which is up 35% year-over-year. And when we initially saw that number this morning, we presumed some of the retro price increases for the acuity mix really had come through and driven that. But it's not what you cited in the release. You said still costs primarily things like cost performance and on the call you’d said still what you're getting from states in terms of rates was not quite as good, or as you had anticipated. So I just wanted to understand that were there not material benefits from some of this acuity true ups happening in the quarter, and if it's not what was really the sources of cost performance?

Gail Boudreaux

Well, thank you very much for the question. I think there's certainly a couple of things embedded in that question. The first is that 2018 was well, as you think about the comparative from 2018 to 2019 and as you go back to our call in that quarter. So you're comparing, I think, quite frankly, a below baseline 2018. So there isn't anything unusual in this quarter for 2019 in our government business. We have made a lot of progress on getting the rates that match the population. So we feel really good about that.

But as you know, this is a complex business with geographies and a population mix. And so we still feel that there's a lot of runway and we're having those conversations in our states. And we are making progress and we are seeing it flow through, but we didn't have a giant retro payment or anything of that sort to point to in this quarter, but we did see improvement in rates and we are seeing improvement in the overall management of the business.

So I guess the summary answer to the question is the comparison. We like where we're heading but we also believe we have a lot more runway and the conversations are quite productive with our states. And we do feel confident. But again, we can't absolutely predict timing. Thank you. Next question, please.

Operator

Your next question comes from the line of Steven Valiquette from Barclays Capital. Please go ahead.

Steven Valiquette

So just on the topic of Medicaid membership, over and above the shifting of Medicaid enrollees into commercial plans that's been talked about previously. I guess, I'm just curious if you can comment on the public charge rule that could create some extra volatility around Medicaid enrollment. And in light of some federal courts and joining the rules, do you think beyond just the notion this could still be material for Anthem either in late '19 and into 2020? Thanks.

Gail Boudreaux

I'll ask Felicia to comment.

Felicia Norwood

In terms of the public charged rule, we haven't seen a material impact on our business year-to-date. However, the rule is still pending. We will continue to monitor this with our state partners. And certainly because of the unknowns, we are cautiously optimistic that we're going to be able to work closely with our partners as individuals are going through this process.

This in some respect is akin to some of the things you see with respect to re-verification. And one of the things that we've been able to do with our state partners is to try to understand early on individuals who have been impacted or maybe impacted, and have an opportunity to work with individuals to maintain their eligibility. So thus far we haven't seen a material impact in our business. But as I said, it's still early. So we will continue to monitor this and work closely with our state partners throughout this process.

Operator

Your next question comes from the line of Lance Wilkes from Bernstein. Please go ahead.

Lance Wilkes

Could you talk a little bit about the partnership strategy with the other blues that are out there? And what you're seeing as far as progress in Medicaid joint ventures, Medicare Advantage, cross sales and specialty? And do the other blues have any sort of changed perspective or greater sense of urgency in any of this given the political dialog and concepts like public option, et cetera?

Gail Boudreaux

As you know, we shared that we are working quite closely with our blue partners across a variety of opportunities. And we're very pleased with partnerships that we have in Medicaid. We have eight alliances today. Five are with our fellow Blue Cross Blue Shield partners. We're also adding additional partnerships. We're adding a Medicare partnership in Louisiana. And we're adding a partnership in Maine with the Maine Health System.

So it's broader than just the blues. I know your question was more specific to the blues. As you saw, we announced that Blue Cross of Idaho will be an IngenioRx customers. So there's another great example. So more broadly, I think we have a broad array of capabilities, both through Medicaid but also through our diversified business group. Our AIMS business and our CareMore businesses work across the spectrum. North Carolina is a great example where we are doing a partnership with Blue Cross Blue Shield of North Carolina for Medicaid. Our CareMore business will be building clinics in that environment as well and then IngenioRx will be the PBM. So to me that offers a really great glimpse of the ability to package things across the Blue.

In terms of overall I think as a system, we're intensely focused on affordability and cost and access for the one in three Americans that we serve across Blue Cross Blue Shield plans. And I think you saw hopefully many of the Medicare focus and advertising that the Blue Cross Blue Shield brand this past year. So I think what you're seeing is that we recognize the rule we have in the American healthcare system. And by working together, we can do a lot more to have an impact on the system.

So thanks very much for the question, but we're very -- quite frankly bullish and excited about the opportunities that as a Blue system, the impact that we can have across America. Next question, please.

Operator

Your next question comes from the line of George Hill from Deutsche Bank. Please go ahead.

George Hill

Just to piggyback on the one that Gary asked earlier, if we think about the expected Medicaid margin improvements in 2020, how much of that is dependent upon the risk for acuity adjustments coming through? And John, I think you talked a little bit about the timing of those tending normally 12 to 18 months, so that would kind of coincide with it kind of seeing the issue in Q2 of next year and it's starting to roll through into 2020. And I'd say just, am I thinking about that right?

John Gallina

In terms of exactly how much is related to the re-verification, well it's certainly a piece of it. But just to be clear, every year, we go through with actuarially justified rates and have rate renewals like rate renewals and negotiations with our states. And so obviously, hitting our target margins requires getting from our portfolio of states that we have of getting the right rates on an overall basis. Clearly, part of that conversation is around re-verification, but that's not the entirety of the conversation. The conversation is really about actuarially justified rates based on the acuity of the population regardless what the starting point is. So in one regard, getting the right rates is the entire issue but it's not just re-verification.

Operator

Your next question comes from the line of Josh Raskin from Nephron Research. Please go ahead.

Josh Raskin

A question around the Medicare advantage starts, I know you mentioned in your prepared remarks that there's a focus on improvement, et cetera. And as we kind of look through the metrics, it looked like drug experience, drug safety categories like that were the ones that show the biggest decline. So I know there's a huge delay and so as Ingenio kind of ramps up in '19 and into '20. Is there an opportunity you think to improve things for next year, or is this going to be a multiyear sort of fix? And as you guys dug in, are there certain metrics that you think you can control shorter term around the MA starts? Thanks.

Gail Boudreaux

As you can -- you've clearly identified some of the areas that we've focused on as well. In terms of your question, as I said, we are disappointed in the results. And we've dug in very deeply to figure out where we can have an impact. Last year, we did make an impact in moving one of our largest contracts, our four-star with that intention and focus. But we know this year part of the issue was just the timeliness of data and our ability to have an impact on some of members in those clinical pharmacy plans now that we remove, we will be moving our entire Medicare advantage business on one-one. We're already very engaged and having an impact.

So yes, we do believe we can have an impact, not only on clinical but we also believe in some of the other metrics where we did make improvements on HEDIS, for example, in many of our markets we still have opportunities there with better data and the integration of the data that I shared with you earlier. And then certainly in some of the consumer metrics, we feel that as part of our end-to-end focus on execution across our businesses that there is opportunity there. So yes, we absolutely believe we can have an impact.

On pharmacy, now owning pharmacy 100% under our own control, we really do believe that will be a multiyear opportunity for us to dramatically expand that. So you hit the core. But as we look at our results this year, the biggest disappointment was in those clinical pharmacy results, which declined. So thank you very much for the question. Next question, please?

Operator

Your next question comes from the line of Scott Fidel from Stephens. Please go ahead.

Scott Fidel

Thanks. Question just is on group Medicare Advantage. And if you can just update us on margins on the class of 2019 business are progressing relative to plan. And then relative to 2020, I know that you've talked about expected continued growth in group MA essentially. But if you can maybe help sort of size that, or just sort of how that's trending relative to the long-term trajectory that you provided for us at Investor Day? Thanks.

Gail Boudreaux

I'll have, Pete, share some perspective on the group Medicare market.

Pete Haytaian

Thanks, Scott. Appreciate the question. As you know, we saw some really nice growth in 2019 in the group retiree business, and we do expect growth to continue into 2020. As we said before and we're seeing this come through, our greatest opportunity continues to be with respect to our inherent pipeline of existing commercial clients that have Medicare wrapped product. And so we're seeing really strong sales there.

As it relates to new store sales and RFPs, the market continues to be really competitive. And we do win some business there as well. But we're also looking at creating new opportunities. So the question was asked before about Blue partnerships, and we see this as another wonderful opportunity for Blue partnerships and we're actually exploring those.

And then finally I'd say having a competitive pharmacy benefit will certainly help in 2020 and beyond as it relates to upcoming bids and group retirees. So overall, we feel good that we'll continue to see growth in that space.

John Gallina

And that business is dilutive when we first say it takes 12 to 18 months of dilution. And so it continues to be a headwind until we get the block of business to an appropriate level.

Operator

Your next question comes from the line of Dave Windley from Jefferies. Please go ahead.

Dave Windley

Josh asked my earlier question, I'm going to ask a follow on to that. I'm thinking about this MA starts and improving net investments and quality. As you think about the $3.2 billion that you have to essentially reinvest in the business. How would you, if you'd be so kind as to tell us. How would you think about allocating that between the benefit design and price point references that I think John gave earlier and then how much would quality investments like stars consume of the $3.2 billion?

Gail Boudreaux

Well, we haven't broken it down in that way. And I guess as we think about this, we're investing heavily in pharmacy, just so you know. I mean, it's not just the benefit of the impact of the earnings that we get because of the lower cost of goods sold, which is really driving that 4 billion that is fundamentally a lower cost of goods sold. But as part of bringing IngenioRx up to speed and the migration, we've built a new integrated specialty clinical service center, which has areas of excellence around these areas that I think will absolutely help our clinical performance and pharmacy.

And again, we know what we need to do. And we have a very clear line of sight around what the opportunities are in pharmacy. And we feel very confident in our ability to have an impact on those. As you think more broadly about pharmacy, I think John has shared with you how we're approaching the $3.2 billion, and it's very different based on each of our lines of business and where we were competitively and how that aligns with plan designs, et cetera. So it's not a straight line formula. But clearly, pharmacy gives us a tailwind as our opportunity in Medicare Advantage and helps us offset some of this impact from stars. Thank you. Next question, please.

Operator

Your next question comes from the line of Sarah James from Piper Jaffray. Please go ahead.

Sarah James

Thank you. I was hoping you could talk about the DBG selling process beyond Ingenio. Just wondering how long the selling process is to better understand how strong the line of sight is into near term sales and some conversations so far. Do you have a sense of what the near term product mix could look like over the next couple of years?

Gail Boudreaux

I think broadly as you think about any group of services businesses, the selling cycles very much vary. Our end AIMS business has been in the market for a very long period of time. Aspire has a very mature sales cycle. And CareMore also is working as part of very much, not just the integrations that we mentioned and the partnerships we have but they've been actively talking to our Blue partners about areas where they can help.

So it isn't a definite. But I'd say generally, as you think about pharmacy, it's 12 to 18 months at least lead time. As you think about large scale projects bringing up a new CareMore sites, you're usually talking nine months plus in terms of the procurement and the discussion. AIM is a shorter sale off, because we can deal with closer capabilities and we're really excited about bring Beacon into the family in the fourth quarter, because we also believe that provide some really unique capabilities.

So overall as we've shared our diversified service business is a growing business. It's something over the next three to four years you're going to see much more significant traction. But quite frankly, we are seeing progress in sales already and we feel really good about that. But I would say at least 12 to 18 months is a lead time in terms of the conversations and the procurement just given these are fairly large sale that we're talking to people about. But thank you very much for the question, and we're very much looking forward to sharing more about DBG as we go forward. Next question, please?

Operator

Your next question comes from the line of Michael Newshel from Evercore ISI. Please go ahead.

Michael Newshel

For exchanges in 2020, can you frame the magnitude of any geographic re-expansion of your planning, and whether that kind of revenue growth could be any meaningful offset to the margin normalization you talked about?

Gail Boudreaux

Pete, please?

Pete Haytaian

We're pleased with our individual performance and progress. And I think our strategy really remains the same with respect to expansion where we're disciplined and we're targeted in terms of where we play. We've talked about this before but it's been largely based upon geographies where we can partner with key providers at the right economics and in partnership on delivering really strong cost of care, partnering with providers and being aligned on risk adjustment. And in many instances, we're focused on obviously leveraging our value based care relationships.

And of course then importantly, we have to be positioned well with respect to our product and being number one and number two as it relates to the right product. And this has translated into good results for us as we talked about earlier, bit better than expected. As we continue down this path in 2020, we're continuing to target expansions. We do see pockets where competitively some of our competitors are little bit better positioned. And if that's the case, we're going to remain disciplined and we're not going to participate in those markets in which we can't do what I said before, and that is partner with providers and have the most competitive product.

So we feel like we're continuing down the path of being very methodical and thoughtful about that business, and we'll continue to grow that business in the right way.

Operator

And your final question today comes from the line of Charles Rhyee from Cowen. Please go ahead.

Charles Rhyee

Just to clarify earlier some of your comments, John, around -- and Gail around the commercial business, these few accounts I know you didn't want to get too much into it. But the reason for termination, it sounds like you're saying is because when you re-price the business for them, those rates were just didn't match up with what I guess clients had wanted. But did that factor in also what expect to say that you would have been able to generate for them through Ingenio? And just to be clear that this shouldn't have any impact on how your commercial book is pricing for next year?

Gail Boudreaux

Well, let me start and then I'll ask John to follow up. First, in terms of the last part of your question, no, we feel really strongly. I mean, we reaffirmed our trend. We feel very strongly about our book of business. And the commercial business is performing. Our margins are good. They're improving. And honestly outside of even just risk, we're adding a lot more specialty products and bringing through revenue in our clinical products. So overall, no, you shouldn't read into anything about our commercial business. In terms of your second question, maybe I'll have John answer that one, because I don't think that there is much more to add.

John Gallina

In terms of the impact on the overall commercial book, really there is not any. Our prior guidance did assume that these members would stay with us for the rest of the year. So it was a difficult decision. So there'll be a slight impact on our year end membership. However, associated with our pricing, with our growth outlooks, with our competitive position and each of our markets, there is really no change. We feel very good about our commercial business strategy and the ability for Pete and the team to execute that. And think that 2020 is going to be another growth year for us. So thank you.

Gail Boudreaux

Thank you very much for all of your questions. And I'd like to thank everyone for hanging in there this morning while we dealt with the phone issues, but we're happy that we were able to address all of your questions and still get everyone through the line.

As you can see, we remain committed to delivering a simple, more affordable and personalized experience for those we serve. And I look forward to building on our momentum in 2020. I want to thank our associates for their ongoing commitment to serving our nearly 41 million members. And I look forward to speaking with all of you again soon. Thank you.

Operator

Ladies and gentlemen, this conference will be available for replay after 11:00 AM Eastern Time today through November 6th. You may access the AT&T teleconference replay system at any time by dialing 1-800-475-6701 and entering the access code 432048. International participants dial 320-365-3844. Those numbers once again are 1-800-475-6701, or 320-365-3844 with the access code 432048.

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