
HEALTH PLAN WEEK

United Crushes 1Q Earnings Consensus, but Profit May Now Be a Double-Edged Sword

UnitedHealth Group on April 20 kicked off the first-quarter 2010 earnings season by pummeling Wall Street's expectations — thanks in part to better-than-expected membership growth, a mild flu season and low utilization rates.

But profitable health plan operators could face increased scrutiny and intensified efforts to hold down premium rate increases, some industry observers warn. The same day that United released its earnings results, the Senate Health, Education, Labor and Pensions Committee coincidentally held a hearing titled Protection from Unjustified Premiums (see story, p. 5).

United reported first-quarter net income of \$1.19 billion (\$1.03 a share), up 21% from \$984 million (81 cents a share) in the year-ago period, and 69 cents better than Wall Street's consensus estimate. Revenue increased about 5% to \$23.2 billion. Citing stronger-than-anticipated revenue growth, the company boosted its full-year 2010 earnings outlook to a range of \$3.15 to \$3.35 per share — up from its earlier projection of \$2.90 to \$3.10.

Although equities analysts had predicted a solid quarter for the insurer (HPW 4/19/10, p. 1), they were surprised by the company's strong performance. In a note to investors, Christine Arnold, an equities analyst at Cowen & Co., called United's earnings results "shockingly strong." The growth was driven by a commercial medical loss ratio of just 79.1% — down significantly from 81.5% in the year-ago period.

Despite some headwinds (e.g., declining Medicare reimbursement and higher COBRA membership), United's 2010 earnings guidance could be higher, says Steve Shubitz, an equities analyst at Edward Jones. "I think their guidance for 2010 remains conservative, especially given the better-than-expected enrollment and potential that this could further improve if employers start hiring again." Based on United's results, there is potential for the rest of the sector to report higher-than-expected commercial enrollment and better prior-period development due to lower-than-expected costs from H1N1 and lower-than-expected utilization, he adds.

Despite the strong first-quarter results, investors were pessimistic. United's stock price ended the day at \$30.94 — down 29 cents from the previous day's close.

At a Senate hearing held the same day, Sen. Tom Harkin (D-Iowa) interrupted the proceedings to note the company's better-than-expected profit. United and WellPoint, Inc., he added, control 80% of the market in Iowa.

"The good news is that WellPoint can breathe a little easier, as it now has a close friend on the public enemies list," Oppenheimer equities analyst Carl McDonald quipped in a note to investors. In February WellPoint faced public scrutiny, as well as a House subcommittee hearing, after deciding to boost rates for some individual plans in California by as much as 39% (HPW 3/1/10, p. 1). "Normally, United's earnings would be a cause for celebration, as the results confirm that fundamentals in the industry are even better than the market's high expectations. Today, though, the earnings report just makes us cringe, because we can't emphasize enough how fragile the political environment for this group still is."

Fred Karutz, general manager of health plan solutions at Silverlink Communications and former corporate vice president at Health Care Service Corp., agreed that the earnings results could shine the political spotlight on United. During an April 20 webinar sponsored by HPW, Karutz said the company's profit was far from outrageous. "Ultimately, this is a low-margin business and insurers are an easy scapegoat" for rising coverage costs. The industry, he added, needs to become more proactive in explaining how rising medical costs, new technologies and pharmaceuticals impact the cost of coverage.

In its earnings release, United seemed to anticipate the ire its results could raise. Prior to stating its net earnings of \$1.2 billion, the release details strategies that would reap a potential \$366 billion in savings by improving quality in Medicaid, a savings of \$332 billion from increased use of technology and \$540 billion in savings from better containment of costs using techniques in private market health programs, Shubitz notes.

While United lost commercial members during the first quarter of the year, losses were lower than anticipated

and could be an early indication that the market is stabilizing. Here's a look at where United saw membership growth and declines this quarter:

◆ **Medicare Advantage:** United's MA enrollment grew by 215,000 members (including 55,000 from Health Net, Inc.), surpassing the company's expectations for the quarter. United has 2 million MA members and late last year predicted it would increase enrollment by 250,000 by the end of 2010.

◆ **Commercial enrollment:** Overall medical membership fell 4% to 24.5 million from the year-ago period,

and declined by 105,000 from the end of the last quarter. However, the decline was less severe than the company had projected. On the commercial risk side, the company reported enrollment of 9.1 million lives, a drop of about 300,000 members from the previous period, but 100,000 fewer than the company had projected.

◆ **Medicaid:** United said its Medicaid enrollment now tops 3 million — up by 145,000 beneficiaries from the prior quarter. ✧