



**MINERVA**  
Investment Management  
Society

**Matteo Canali** (Equity Research Analyst)  
**Cataldo D'Imperio** (Equity Research Analyst)  
**Marco Di Pisa** (Equity Research Analyst)  
**Marco Guglielmini** (Equity Research Analyst)  
**Valentina La Barba** (Equity Research Analyst)  
**Mattia Lentini** (Equity Research Analyst)

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# UNITEDHEALTH GROUP

Listed on: New York Stock Exchange  
Ticker: UNH:US (BB), UNH.N (TR)

## Our View:

We suggest a **STRONG BUY** recommendation on UnitedHealth Group INC, stating a \$266,41 target price, with a closing price of 219,07 by 27<sup>th</sup> March.

We assess our positive stance on the stock as we appreciate the company's strong track record. We believe this could continue in the coming years thanks to the combination of its strategy of continuous innovation-driven investments, increasing diversification both geographically and by verticals, employee satisfaction levels and a very solid underlying market.

## Key Points:

UNH increased prior EPS guidance by 16% from \$10.55-10.85 to \$12.30-12.60, as it lowered tax rate guidance from 37% to 24% and accounted for rising returns from data analytics/technology investments, while no changes in its cost trend is expected.

## Valuation:

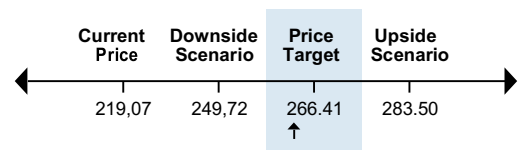
Our valuation is the combination of a three-stage DCF analysis (5 years of business plan and two terminal value) and a multiple valuation based on P/E and EV/EBITDA. The final result is obtained as mean value of the price ranges obtained from each methodology.

# STRONG BUY

Price: \$219.07

Target price: \$266.41

## SCENARIO ANALYSIS



## KEY STATISTICS

<b>52-Week Range</b>	\$223.750 - 227.82
<b>Average Volume</b>	3.328.596
<b>Shares Out. (mm)</b>	967,66
<b>Market Cap. (mm)</b>	\$217.460

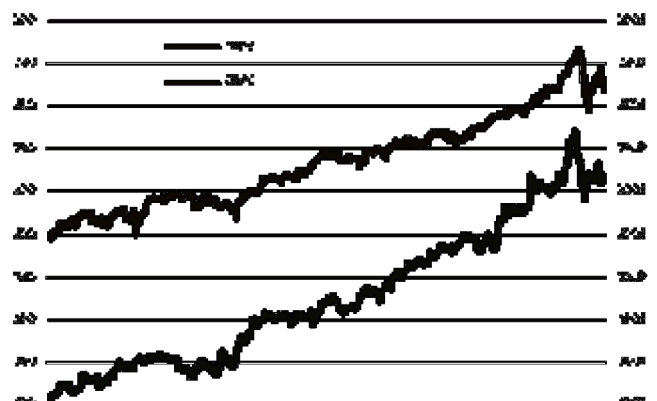
## MINERVA ESTIMATES

	Y2017	2018E	2019E	2020E
<b>E (mm)</b>	10.558	14.330	15.809	17.385
<b>EPS</b>	10,72	14,58	16,25	17,77
<b>P/E</b>	20,6x	18,0x	16,0x	15,1x

## PROFILE

<b>Sector</b>	Health Services
<b>Industry</b>	Managed Healthcare
<b>President, CEO</b>	David Scott Wichmann
<b>CFO</b>	John Franklin Rex
<b>Headquarter</b>	Minneapolis Minnesota

## 5Y TRF VS S&P500 DAILY PERFORMANCE





## UNITEDHEALTH GROUP OVERVIEW

UnitedHealth Group is a diversified health company which provides clients with healthcare services through resources and clinical expertise in order to improve the well-being of local communities. Its headquarter is in the USA, precisely in Minnetonka, Minnesota. It is the first healthcare company by revenues, serving more than 115 million individuals worldwide, bringing innovative applications, services and products. Their core abilities in clinical competence, advanced technology and data and health advice allow the firm to accommodate the requirements of a developing healthcare environment. As a matter of facts, more than \$3.3 billion are invested in technology and innovative products and services. Moreover, the high number of physicians and nurses (more than 30.000) worldwide help clients live healthier lives.

The company operates in all 50 states of the USA and in more than 130 other countries, handling more than 750 billion digital transactions each year. Recently, in the beginning of 2011, the company had undergone an enterprise reorganization in order to exploit the opportunities in the United Kingdom Government's NHS reforms. Today the company is split in 2 sub-companies: Optum, which operates solely in the UK and provides technology and information regarding health services, and UnitedHealthcare, which produces health coverage and benefits services.

Optum is divided in 3 divisions: OptumInsight, OptumRx, Optumhealth. UnitedHealthcare is divided in four divisions: UnitedHealthcare Employer & Individual, UnitedHealthcare Community & State, UnitedHealthcare Medicare & Retirement, UnitedHealthcare Global.

The major acquisitions that took place in early 1990's allowed the company to be one of the most important health care providers in the USA. For instance, it acquired firms such as HealthWise of America, which operated in Arkansas, Maryland, Kentucky and Tennessee, HealthPartners of Arizona and Touchpoint Health Plan, based in Wisconsin. After the year 2000, the company started to merge with health insurance firms such as Medicaid insurance company AmeriChoice and Mid Atlantic Medical Services, which provides insurance services in the states of Washington D.C, Maryland, Delaware, Virginia and West Virginia. Recently, UnitedHealth group was involved in many big M&A operations (e.g. DaVita Medical Group for \$4.9 billion and Banmedica for \$2.8 billion).

UnitedHealth Group was involved in legal issues for backdating of stock options, after some probing stories published in the Wall Street Journal. The law suit brought the CEO of the company to resign. The SEC, the IRS and the prosecutors in the U.S. attorney's office for the Southern District of New York began investigating in this matter in 2006. After a year the SEC announced a partial settlement under which the CEO McGuire will pay \$468 million. Other lawsuits regarded a fraud by Ingenix toward the United States by boosting risk adjustment scores and rates found in a database of health care charges kept by Ingenix (a subsidiary) were lower than what the actual cost of certain medical expenses was.

Nevertheless, the firm had presented an always increasing net income and ROE and also our forecast sees a continuous enhancement of these financial data as well as a continuous growth in free cash flow to firm and free cash flow to equity.

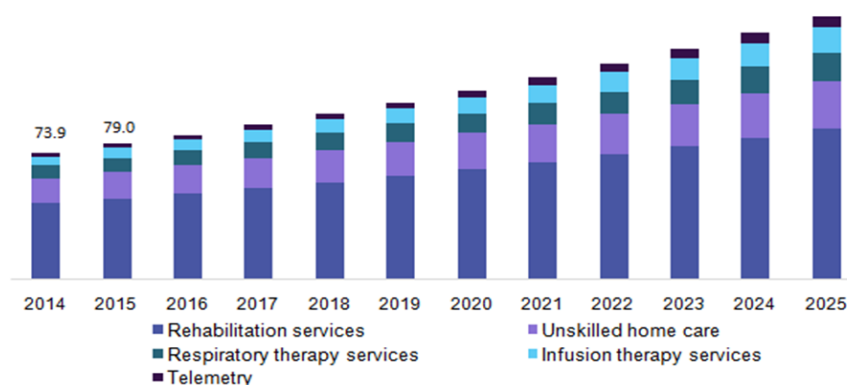
Furthermore, our industry analysis reveals which are the main drivers for the healthcare sector: expenditures on three causes of death and investments in new technologies. After all, we believe that UNH stocks will trade at a relatively higher price than its comparable companies, due to its outstanding empirical and expected performance.

## GLOBAL HEALTH CARE SECTOR

Private health companies have been suffering revenue pressures and declining margins for years, the trend is believed to persist as increasing demand, infrastructure upgrades, and therapeutic and technology advancements strive the already limited financial resources. As a result, global health care main drivers will be:

- Expenditures on three leading causes of death: cardiovascular diseases, cancer and respiratory diseases. Furthermore number of diabetes sufferers is expected to rise from the current 415 million to 642 million by 2040: this elements will lead to an improvement of costs of health care's companies.
- Investments in exponential technologies to reduce costs, increase access, and improve care: Exponentials will rewrite health care by affecting areas such as synthetic biology, 3D printing and the use of Artificial Intelligence; indeed three-quarters of healthcare executives plan to invest in AI in the next three years but many lack the ability to implement this kind of technology, according to PwC. Only 20 percent of respondents said they had the technology to prosper with AI.

### The impact of different units



Source: Grand View Research

The global home healthcare market size was valued at USD 244.4 billion in 2015 and is expected to grow at a rate of 10% over the forecast period. The rising of treatment cost is one of the biggest area of concern among government and health organizations, and these organizations are attempting to control the increase of health cost.

Home healthcare is a cost-efficient alternative to expensive hospital stays. For instance, treatment cost for acute care hospital is around USD 3,250.0 per day. On the contrary, home care cost is approximately USD 50.0 per day. These settings help to save cost significantly hence, anticipated to serve as high impact rendering driver for the home healthcare market.

The growth of geriatric population is one of the main driver for the expansion of the market, indeed the geriatric population is expected to be more than double from 7.0% to 16.0% in 2050. This demographic group is susceptible to chronic diseases which require long term care.

The foundation and the maintenance of hospitals and other such settings are capital intensive in nature and require large investments in terms of capital and operational expenses. Therefore, providers with the help of mergers and acquisitions are now entering the rapidly growing home healthcare market in an attempt to take advantage on the available opportunities and contain costs.

## DCF VARIABLES' BASIS ANALYSIS

### KEY FIGURES

In the following table there is the key factors and, each one, the percentage variation compared to the previous year.

	2013	2014	2015	2016	2017
<b>Revenues</b>	121.744	129.695	156.397	184.012	200.136
		6,531%	20,588%	17,657%	8,762%
<b>EBITDA</b>	10.998	11.752	12.714	14.985	17.454
		6,856%	8,186%	17,862%	16,476%
<b>EBIT</b>	9.623	10.274	11.021	12.930	15.209
		6,765%	7,271%	17,321%	17,626%
<b>Profit before taxes</b>	8.915	9.656	10.231	11.863	14.023
		8,312%	5,955%	15,952%	18,208%
<b>Net Income</b>	5.673	5.619	5.868	7.073	10.823
		-0,952%	4,431%	20,535%	53,019%
<b>EBITDA Margin</b>	9,034%	9,061%	8,129%	8,143%	8,721%
		0,305%	-10,285%	0,174%	7,093%
<b>EBIT Margin</b>	7,904%	7,922%	7,047%	7,027%	7,599%
		0,220%	-11,044%	-0,285%	8,149%
<b>Profit Before Taxes Margin</b>	7,323%	7,445%	6,542%	6,447%	7,007%
		1,672%	-12,135%	-1,450%	8,684%
<b>Net Income Margin</b>	4,660%	4,332%	3,752%	3,844%	5,408%
		-7,024%	-13,398%	2,446%	40,691%
<b>EPS</b>	5,69	5,89	6,11	7,38	10,91
		3,515%	3,735%	20,786%	47,832%
<b>DPS</b>	1,0525	1,405	1,875	2,375	2,875
		33,492%	33,452%	26,667%	21,053%
<b>BVPS</b>	32,5	34,03	35,59	40,24	49,37
		4,708%	4,584%	13,065%	22,689%
<b>D/E</b>	0,52	0,54	0,95	0,86	0,66
		3,846%	75,926%	-9,474%	-23,256%
<b>Debt/EBITDA</b>	1,53301	1,48111	2,52430	2,20020	1,81574
		-3,385%	70,433%	-12,839%	-17,474%
<b>Interests cov</b>	13,59	16,62	13,95	12,12	12,82
		22,296%	-16,065%	-13,118%	5,776%
<b>ROE</b>	17,50%	17,31%	17,18%	18,33%	22,10%
		-1,086%	-0,751%	6,694%	20,567%
<b>NFP variation</b>	-3470	-5290	12360	-754	-3440
<b>Capex</b>	-1310	-1530	-1560	-1710	-2020
		16,794%	1,961%	9,615%	18,129%

Between 2013 and 2017 the company witnessed an increase in revenues. The increase in NOPAT was partially reduced by an increase in the Net Working Capital and an increase in the Capex, which enabled the company to grow over the years. Since the NOPAT is higher than all the other items, in those years the company realized a positive Free Cash Flow to Firm value. Therefore, it is expected that with the investments of the previous years the company will be able to generate a more than positive NOPAT. This will also lead to an increase in the Net Working Capital and the Capex, then the increase in quantities sold will lead to an increase in trade receivables and payables. Since in order to sustain growth, the company will need new investments we have assumed that the growth rate of Capex and amortization is equal to 10% in both cases. This value is however lower than the historical growth rates of Capex due to the fact that most of the investments were made in the years 2016 and 2017. Since in the previous years investments have increased, in the following years will also increase depreciation on those same assets.

### Historical FCFF

	2013	2014	2015	2016	2017
Net Income	7.297	7.046	7.659	9.612	12.917
Interests	460	375	367	629	875
delta CCN	-306	1005	2081	183	679
Capex e DD&A	-1307	-1525	-1556	-1705	-2023
FCFF	6.144	6.901	8.551	8.719	12.448

### Forecast FCFF

In order to estimate FCFF of 2018-2022, we have calculated the average growth rate of both Capex and DD&A: it is 10%.

	2018	2019	2020	2021	2022
NOPAT	26443	30580	36522	41461	42345
Delta CCN	-8622	-10888	-13512	-16358	-17123
Capex	-2470	-2716	-2988	-3287	-3616
DD&A	-2222	-2444	-2689	-2957	-3253
FCFF Forecast	13130	14531	17333	18859	18353

## VALUATION ANALYSIS DCF

In our valuation, we perform a three stage DCF analysis. The first stage cover the business plan period, the second one concerned the year 2023/2028 and the third one is the terminal value.

Firstly, we have identified the Free Cash Flow To Operation based on Business Plan provided by the management. After that we have expanded the FCFF horizon until the 2022. Our estimate for FCFF, after the management plan, it is estimated with decreasing growth rate, which converge toward the mean average of the industry in the mid-long run.

YEARS	FCFO	ΔFCFO
2019	14531,1	10,6%
2020	17333	19,2%
2021	18859	8,8%
2022	18353	-0,2%
2023	19637,7	7,0%

After that we focused on the estimate of the cost of debt and on the cost of equity. In order to assess it, we have analyzed the annual interest rate on commercial paper and long-term bond issued by the company and not yet repaid.

INTEREST RATE	DEBT AMOUNT		
1,5	150	3,1	2108
6	1106	3,45	1007
1,9	1501	3,38	776
1,7	747	2,95	642
1,63	497	4,63	947
2,3	501	5,8	1165
2,7	1517	6,5	1105
3,88	467	6,88	698
1,95	892	5,7	923
4,7	425	5,95	1596
2,13	744	4,63	389
3,38	516	4,38	466
2,88	760	3,95	685
3,35	1114	4,25	555
2,38	1033	4,75	650
-	891	4,2	822
2,75	12	4,25	2362
2,88	626	3,75	808
3,75	759	6,63	798
			<b>33,729</b>

The weighted-average interest rate based on data is 3,89%.

For the cost of equity we have used the CAPM as a model. First of all we have computed the risk free rate based on the unweighted average of bid yields on all outstanding fixed-coupon U.S. Treasury bonds neither due or callable in less than 10 years (risk free return proxy) and the result is  $R_f=3,11\%$ .

The expected rate of return on the market portfolio using the historical series of returns of the S&P500 is 12,63%.

The estimate of  $\beta$  is based on a linear regression of the returns of the stock with those of the market index.

Variance UNH	21.01
Variance S&P500	7.32
Covariance (UNH, S&P500)	5.01
Correlation coefficient (UNH, S&P500)	0.4
$\beta$	0.68
$\alpha$	1.6

Using the CAPM model the cost of equity is equal to 9,63%, very close to numerous estimates made by analysts of primary investment banks. The last variable to be estimated for the use of the DCF evaluation method is the growth rate  $g$ . We estimated a differentiated growth rate. In the 2023 the rate of growth in profits was estimated according to the retention rate and the return on invested capital ( $RR \times ROIC=8,05\%$ )

and in the following years the growth rate decreases constantly to the normalized estimate of the growth rate of the American pharmaceutical industry ( $g_2 = 2,5\%$ ).

Actual values are calculated in 2018.

Net Financial Position is measured at today market value.

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
FCFO	13130	14531	17333	18859	18353	19638	20816	21857	22731	23413	23998
Actual FCFO	13130	13380	14697	14724	13194	13000	12689	12268	11748	11143	10517
TV											393415
Actual TV	172406										
EV	312896										
NFP	33729										
Equity Value	279167										

### Sensitivity analysis of Terminal Value in 2028

	1,5%	2,0%	2,5%	3,0%	3,5%
6,6%	248335,2	275328,1	308904,7	351808,1	408551,4
7,6%	189115,8	206001,2	226197,4	250784	281367,5
8,6%	148123,5	159344,9	172406	187799,4	206211,1
9,6%	118465	126258,7	135150,2	145388,8	157305,9
10,6%	96291,46	101889,8	108179,3	115296,4	123415,8

### Sensitivity analysis of Actualized Terminal Value in 2018

	1,5%	2,0%	2,5%	3,0%	3,5%
6,6%	248335,2	275328,1	308904,7	351808,1	408551,4
7,6%	189115,8	206001,2	226197,4	250784	281367,5
8,6%	148123,5	159344,9	172406	187799,4	206211,1
9,6%	118465	126258,7	135150,2	145388,8	157305,9
10,6%	96291,46	101889,8	108179,3	115296,4	123415,8

### Sensitivity analysis of Enterprise Value

	1,5%	2,0%	2,5%	3,0%	3,5%
6,6%	402024,4	429017,3	462593,9	505497,4	562240,6
7,6%	335965,6	352850,9	373047,1	397633,8	428217,2
8,6%	288613,2	299834,7	312895,8	328289,2	346700,9
9,6%	253033,5	260827,3	269718,7	279957,4	291874,5
10,6%	225340,8	230939,2	237228,7	244345,7	252465,2

### Sensitivity analysis of Equity Value

	1,5%	2,0%	2,5%	3,0%	3,5%
6,6%	368295,4	395288,3	428864,9	471768,4	528511,6
7,6%	302236,6	319121,9	339318,1	363904,8	394488,2
8,6%	254884,2	266105,7	279166,8	294560,2	312971,9
9,6%	219304,5	227098,3	235989,7	246228,4	258145,5
10,6%	191611,8	197210,2	203499,7	210616,7	218736,2

### Range of price derived from DCF analysis

380,6	408,5	443,2	487,5	546,2
312,3	329,8	350,7	376,1	407,7
263,4	275,0	288,5	304,4	323,4
226,6	234,7	243,9	254,5	266,8
198,0	203,8	210,3	217,7	226,0

This corresponds to a target price of 288\$ per share, which corresponds to a potential upside of the title of the 22% using discounted cash flow method.

## RELATIVE VALUATION

### Peer Group - Absolute Performances

Stock	Price	CCY	Mkt Cap	1Y	6M	3M	1M	1Y	6M	3M	1M
UNH UnitedHealth Group	226,52	USD	217,46	168,01	199,58	222,27	220,96	34,8%	13,5%	1,9%	2,5%
ANTM.N Anthem Inc	231,11	USD	58,51	166,18	197,43	226,02	231,71	39,1%	17,1%	2,3%	-0,3%
AET.N Aetna Inc	178,64	USD	57,62	132,81	162,83	181,57	176,39	34,5%	9,7%	-1,6%	1,3%
CI.N Cigna Corp	194,25	USD	42,41	152,19	184,56	209,16	193,77	27,6%	5,3%	-7,1%	0,2%
HUM.N Humana Inc	273,29	USD	38,59	217,79	258,75	253,03	265,32	25,5%	5,6%	8,0%	3,0%
CNC.N Centene Corp	101,71	USD	17,3	69,56	89,08	99,7	101,66	46,2%	14,2%	2,0%	0,0%
WCG.N WellCare Health Plans Inc	194,47	USD	8,54	143	175	205,5	194	35,9%	10,8%	-5,4%	0,4%
Mean Performance	195,58			146,94	178,02	195,83	193,76	33,1%	9,9%	-0,1%	0,9%
SPX S&P 500	2727,0			2364,87	2465,1	2659,99	2619,55	15,3%	10,6%	2,5%	4,1%

Source: Thomson Reuters, IBES Estimates

### Peer Group – Multiple Comparison

Stock	Price	CCY	Mkt Cap (B's USD)	EV/Sales 18E	EV/Sales 19E	EV/Ebitda 18e	EV/Ebitda 19E	P/E 18E	P/E 19E
UNH UnitedHealth Group Inc.	226,52	USD	217,46	1,1	0,85	12,9	12,25	18	14,34
ANTM.N Anthem Inc	231,11	USD	58,51	0,9	1,06	12,6	10,96	15,8	14,91
AET.N Aetna Inc	178,64	USD	57,62	1,1	1,02	11,5	9,35	16,7	13,60
CI.N Cigna Corp	194,25	USD	42,41	1,1	0,75	9,9	12,16	15,3	17,04
HUM.N Humana Inc	273,29	USD	38,59	0,8	0,35	12,8	7,91	19,7	13,72
CNC.N Centene Corp	101,71	USD	17,3	0,4	0,50	8,7	11,21	15,6	17,57
WCG.N WellCare Health Plans Inc	194,47	USD	8,54	0,5	0,47	11,1	11,21	20,2	17,57
Mean Performance				0,80	0,69	11,10	10,47	17,22	15,73
S&P 500				2,28		17,8		18,8	
Median				0,85	0,63	11,30	11,08	16,25	15,97
75th percentile				1,05	0,95	12,33	11,21	18,95	17,43

Source: Thomson Reuters, IBES Estimates





### Estimates Comparison with Consensus

2018E (USD M's)	Consensus	Minerva Estimates	%diff
EPS	12,6	14,58	16%
EBITDA	21.300	22.800	7%

Source: Minerva estimates and Factset Consensus Estimates

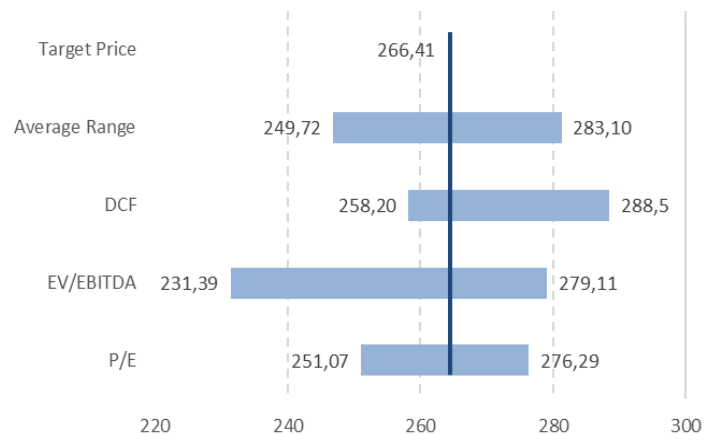
UnitedHealth Group Inc. is expected to trade at 18x P/E (a premium of 11% on the median of its peers) and 12,9x EV/EBITDA (a premium of 14% on the median its peers).

While we acknowledge that the stock is not cheap, we believe UNH to trade at a premium to peers for its outstanding track record, reporting solid results quarter-after-quarter, and stronger fundamentals than 70% of its comparables. We revised upwards EPS company guidance as UNH provided positive earnings surprises in its all recent announcements.

Its increasingly diversified revenue base by end market and geographical area is aiming to provide additional momentum for this trend through M&A deals.

Our analysis lead to consider as a low-high scenario P/E the mean 2018 estimate PE of our peers and a value representative of the 75 percentile of our sample. As a worst case EV/EBITDA we choose the median 2018E PE and as a best case a further premium of 18% on the median of its peers).

	Worst Case	Best Case
P/E 2018E	17,22	18,95
EPS 2018E	14,58	14,58
Price Range	251,07	276,29
EV/EBITDA 2018E	11,3	13,325
EBITDA 2018E	22.800	22.800
NFP 2018	33.729	33.729
N.Shares outst.	967,66	967,66
Price Range	231,39	279,11
DCF	258,2	288,5
Average Range	249,72	283,10
Target Price	266,41	

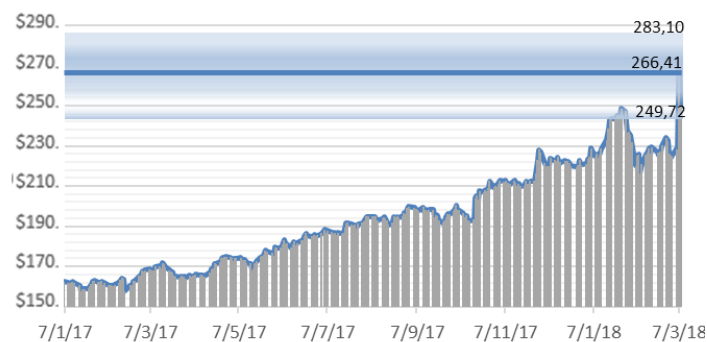




## VALUATION CONCLUSION

Target price is a mean value of the range resulting from a weighted average of absolute and relative valuation (50% DCF, 25% PE, 25% EV/EBITDA), in order to capture intrinsic upside drivers, and implied value from prosperous managed healthcare market.

With a potential 18% gain by year end, our recommendation is a **STRONG BUY** case on UnitedHealth Group.



Source: Minerva elaborations from Thomson Reuters data

## RISK FACTORS

Participation in various government health care programs, both as a payer and as a service provider to payers, brings exposition to additional risks associated with program funding, enrollments, payment adjustments, audits and government investigations.

Regulatory and operational risks and uncertainties from pharmacy care services, that may differ from the risks of other businesses.

Reputational damage due to litigation related to health care benefits coverage, payment and tort claims.

Failure to estimate, price for and manage medical costs in an effective manner, could lead the profitability of our risk-based products and services to decline.

Failure to manage successfully strategic alliances or acquisitions and other significant strategic transactions or relationships domestically or outside the United States, including the retention of a network of independent producers and consultants, physicians, hospitals and other service providers.

Compliance with applicable privacy, security and data laws, regulations and standards, including with respect to third-party service providers that utilize protected personal information.

Adverse market conditions, affecting revenues and investment portfolio.