This presentation is based on my personal views as an analyst.
Sell Side Equity Research

- What it takes to be a Sell-Side analyst
- How my role as a sell-side analyst has changed over time
- My outlook for the future
  - Great time to enter business
  - High turnover presents opportunity
It takes Both Sides of Brain

- Passion for Investing
- Resourceful & Efficient
- Analytical
- Effective Communicator
Passion for Investing

- Career Advice: Follow your Passion

- Also a Passion for Industry Following
  - Healthcare 15% of GDP, Changing, Important
  - Health Benefit Providers at Vortex & Agents of Change

- Fundamental Discipline
  - Value of Firm = Discounted Free Cash Flow

- Be Aware of other Investing Styles, Time Horizons & Imbalances
  - Near-term Supply & Demand for Shares of Stock
  - Trader vs. Investor
US Healthcare 15% of GDP & Growing

Source: Health Care Financing Administration and Bureau & SB estimates.
Intermediaries in $2.0 Trillion Industry

Buyers
U.S. Population 300 million

- Uninsured 44
- TRICARE 8
- Medicaid 44
- Medicare 44
- Individual 17
- Employer 146

Managed Care
- Aetna
- CIGNA
- UnitedHealth
- Blue Cross & Blue Shield
- 1000+ Others

Suppliers
- Physicians
- Hospitals
- Labs
- Pharmacies

Premiums or fees paid by employers & government
85% of premiums passed through to providers

* Uninsured pay for care out-of-pocket and/or receive government and charity subsidized care.
Source: Company data, Smith Barney Research estimates.
Resourceful & Efficient

- Start with "Weak" form of Efficient Market Hypothesis
  - All past data fully reflected in securities prices

- What is New or Different This Time?

- Find New Information &/or Form New Mosaic
  - Before Somebody Else Does & Market Discounts

- Know your Business Cycle
  - Look at Appropriate Time Horizon
  - Often It Exceeds Many Investment Horizons
Example: 6-Year Cycles 1965 - 1993

Source: BCBS Association & SB Research
2000: Forward P/E 60% Discount vs. S&P
Market Expects History to Repeat for Managed Care & Sees “New Economy”

Prices as of April 14, 2005.
Source: FactSet, Smith Barney Research estimates.
6 Yrs of Sideways, Record Market

(a) Managed Care Companies: AET, CI, CVH, HNT, HNT, PHS, SIE, UNH, WC, and WLP, including predecessors CBZ, MME, OHP, TGH, FHCC and WLP (pre-ATH).

Prices as of April 14, 2005.
Source: FactSet, Smith Barney Research estimates.
What Industry Insiders Saw

- Why the Cycle Existed?
  - Non-profit and Mutually-owned Dominated
  - Excess Capital Given Back in form of Premium Cuts

- What Changed?
  - Non-profit and Mutually-owned Health Insurers Converting

- Upshot
  - Business Cycle Elongated, Soft Landing
Elongated Cycle, Expect Soft Landing

Source: BCBS Association & SB Research
2005: P/E Closer to Market Multiple

Prices as of April 14, 2005.
Source: FactSet, Smith Barney Research estimates.
Index up 5x From Trough

(a) Managed Care Companies: AET, CI, CVH, HNT, HNT, PHS, SIE, UNH, WC, and WLP, including predecessors CBZ, MME, OHP, TGH, FHCC and WLP (pre-ATH).

Prices as of April 14, 2005.

Source: FactSet, Smith Barney Research estimates.
Resourceful

- Street was Focused on Technology

- Ground Swell of Conversions & Demutualization
  - Helps to be expert at industry
  - Helps to have industry contacts
Analytical

◆ Basic Problem Solving In Dynamic Environment
  – Gather Facts Resourcefully & Efficiently
  – Analyze Facts to Form Conclusion or “Mosaic”
  – Repeat

◆ Use History as a Lesson NOT as a Guide

◆ Common Pitfalls
  – Assuming Street is Correct on Valuation
    • Don’t lose Discipline Just Because Street Does (dot com)
  – Copying “homework”, be Original & Creative
    • It is by definition too late if you use ideas of others
  – Always taking Contrarian's Stance
    • Sometimes Consensus is Right!
Analytical: Medicare Privatization

◆ Possibly the Largest privatization of our time
  • $400-$500 Billion New Revenue Opportunity
  • 10x Revenue of Largest in Industry

◆ Clearly Can’t use History as Guide
  • Brand new market opportunity
  • Rely on ability to forecast new growth & profitability

◆ Opportunity for Primary Research
  • Helps to be Industry Expert with sources in D.C.
HSA: Asset Accumulation Vehicle

HSA is to healthcare what 401(k) is to Retirement

HSA Product Design

80% 20%

$4,500 Deductible

HSA: Deposit $4,500/yr

Balance after 10 Years

FSA: Deposit $2,000/yr

$2,000

$53,135

Source: Smith Barney Research.
Analytical: Hello H.S.A.

- Health Savings Account
  - Signed into law end of 2003
  - To Healthcare what 401(k) was to retirement

- Will Create Winners and Losers

- Again, Can’t Use History as Guide
  - Understanding of industry to predict winners & losers
  - Understanding of History as Lesson
    - 20 yrs for HMOs & 401(k) to reach 80% Penetration
  - But History Not a Guide
    - 70% of Employers somewhat or very likely by 2006
Effective Communicator

- An Idea is Good If Investors Act on it

- Investors are Inundated with Information
  - But Never Have Enough Good Investing Ideas

- Written, Oral, Telephonic
  - Start with Conclusion – Opposite of How Problems are Solved
  - Titles & Phrases That Concisely Tell The Story
    - “Elongated Cycle, Soft Landing”
    - “Hello H.S.A., Goodbye H.M.O.”
    - “Medicare Handoff Elongates Cycle”
Effective Communicator

◆ Communication Should Be Two Ways
  • Only way to know what is Discounted By Street

◆ Sometimes Ideas Don’t Work
  – Ideas that Work are of course Ideal
  
  – Ideas that Doesn’t Work Aren’t Necessarily Bad
    – If 80% Chance Something Works, Don’t Let 20% Hold you Back – But Be Clear on Risks
    – Be Right > Half The Time

  – Communicate Failures Well
    – Understand What Went Wrong
How My Role has Changed

- Less Time on Capital Formation

- Greater Demand from Trading-Oriented Clients
  - Many New Clients, Increased Demand for My Time
  - Focus on Near-term vs. Long-term Performance
  - Client Turnover, High Hedge Fund Failure Rate

- Reg FD
  - Less Information Flow from Companies
    - Less Leverage over Relationships with Managements
  - Opportunity to Leverage Long-time Industry Sources
    - Net Positive for Good Analysts
My Outlook for the Future

- Great time to Enter the Business & Get Established
  - Challenging Post-Bubble Market
  - Position Well for Next Cycle Turn

- Treat Career Like Investment: Avoid Following the Herd

- Great Jumping Off Point
  - To Industry
  - To Buy-Side Mutual, Hedge, Private Equity, VC, etc.
  - To Investment Banking
  - To Retirement!
Disclosures

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<table>
<thead>
<tr>
<th>Smith Barney Equity Research Rating Distribution</th>
<th>Buy</th>
<th>Hold</th>
<th>Sell</th>
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<tr>
<td>Data current as of 31 March 2004</td>
<td>36%</td>
<td>45%</td>
<td>19%</td>
</tr>
<tr>
<td>Smith Barney Global Equity Research Coverage (2,326)</td>
<td>48%</td>
<td>44%</td>
<td>34%</td>
</tr>
</tbody>
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% of companies in each rating category that are investment banking clients

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