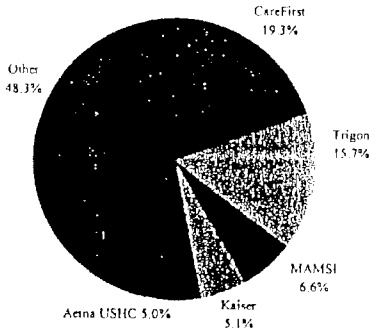
WHY ACT NOW? (CONT'D)

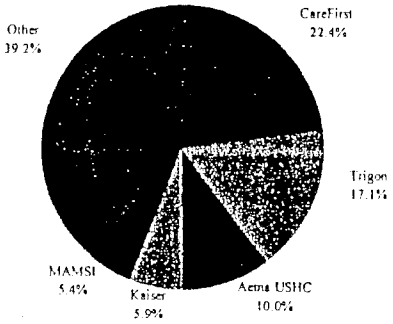
The effects of industry consolidation are readily apparent in Chesapeake's home market.

- Within Chesapeake's home market, competition has increased over the last several years
  - Top five players represented 60.8% of market at the end of 1999 compared to 51.7% in 1997
  - Over the same period Aetna USHC has doubled its share to 10.0% of the total market, positioning as the third largest player in Chesapeake's home market

1997



1999



Source: NRC data provided by CareFirst.
Note: Home market includes Maryland, D.C., Delaware and Virginia.

OCC 015084

WHY ACT NOW? (CONT'D)

In addition, there are several other issues which will ha ve a direct impact on Chesapeake's market position in the near future.

- **Larger competitors are more likely to pursue strategic transactions as their stock prices continue to appreciate and potential transactions become more ac retive to earnings**
  - National and regional plans are looking for market consol ation opportunities (*i.e.* MAMSI, Coventry, etc.) since larger acquisitions may face potential anti-trust issues
  - WellPoint is likely to pursue acquisitions more aggressive once Cerulean acquisition is resolved (currently expected to close by December 2000)
  - As stock prices rise, larger competitors are likely to turn a ay costly share repurchases and redeploy capital strategically
- **Potential to lose control of destiny if competitors exec te strategic combinations away from Chesapeake**
  - Trigon has publicly stated that it intends to pursue a strate c transaction
  - Given potential synergies, Chesapeake is the best merger p rtner
  - However, if a transaction with Chesapeake cannot be com eted, Trigon would likely turn to BCBSNC as its next best alternative
  - WellPoint also remains a possible partner
  - In either case, Chesapeake's market position would be neg tively impacted
- **Peak of industry profit cycle**
  - Scale is required to profitably weather eventual downturn pricing cycle and increased market competition
- **Social purpose of Foundation**
  - Ability to significantly benefit underserved constituencies rough funding of large, dedicated health care foundation

OCC 015085

WHAT HAPPENS IF WE DON'T ACT NOW?

If Chesapeake fails to capitalize on its first mover advan age, several other competitors may enter into transactions which will have dramatic consequences on Chesapeak s local market position.

Potential Combination		Consequences to Chesapeake
WellPoint / Trigon	ς Adds to WellPoint's growing presence in th acquisition experienced competitor next d	Southeastern and Mid-Atlantic region and places a growth-oriented and r
	ς Reduces the number of potential merger par	ers to other smaller non-public BCBS and non-BCBS plans
	ς Smaller partners limit Chesapeake's ability marketplace	gain economies of scale and maintain competitive positioning in consolidating
	ς Significantly reduces the ability of Chesape	e's Board and management to control future strategic combinations
Trigon / BCBS NC	ς Creates contiguous regional market leader	
	ς Reduces the number of potential merger par larger acquirors (such as WellPoint) over w	ers to other smaller non-public BCBS and non-BCBS plans or significantly ich Chesapeake's Board and management would have little control
	ς Smaller partners limit Chesapeake's ability marketplace	gain economies of scale and maintain competitive positioning in consolidating
	ς Increases the attractiveness of the Southeast could gain a significant market presence th	n and Mid-Atlantic region to larger BCBS plans such as WellPoint which ugh the acquisition of a single large (and presumably public) entity
	ς Significantly reduces the ability of Chesape	e's Board and management to control future strategic combinations
Aetna / MAMSI	ς Entrenches well-capitalized and large comp	itor in Chesapeake's core local market
	ς Acquisition is of greater value to Aetna, whi local market leader	n is seeking to build market share, than to Chesapeake, which is already the
	ς Large national competitor could subsidize lo	ses in local market operations to gain additional market share
	ς Coupled with recent acquisitions of NYLCa competition	and PruCare, acquisition would significantly heighten local market
Aetna / Kaiser	ς Entrenches well-capitalized and large comp	tor in Chesapeake's core local market
	ς Acquisition is of greater value to Aetna, whi local market leader	n is seeking to build market share, than to Chesapeake, which is already the
	ς Large national competitor could subsidize lo	ses in local market operations to gain additional market share
	ς Coupled with recent acquisitions of NYLCa competition	and PruCare, acquisition would significantly heighten local market

OCC 015086

DO WE REALLY NEED ACCESS TO CAPITAL?

If Chesapeake intends to preserve its position as a leading regional health care payor, significant capital investment will be required.

($ in millions)

Activity	Investment(1)
ς eCommerce	$ 0-$50
- Partnerships/interconnectivity	
ς New products	$1 0-$250
- Entering new metro markets with Next Generation Consumerism products	
- Call center	
ς Information management system	$ 0-$120
- Integrated IT platforms	
- Medical management tools	
- Reforming networks	
- Revamping provider contracts	
- Bringing on new talent	
- Organization structure change	
- Restructure broker relationships	
Sub-Total ("Infrastructure")	$2 0-$420
ς Mergers	$8 0-$900
- Merger integration	
- Contingency for price wars and acquisitions	
- Total	$1,0 0-$1,320

(1) Estimates from Chesapeake management and Andersen Consulting.

OCC 015087

WHY CAN'T WE FUND OUR CAPITAL NEEDS INTERNALLY?

Without public currency, Chesapeake's capital sources are limited to internally generated free cash flow and external debt financing which can satisfy slightly more than half of the Company's future capital needs.

- DLJ's review of Chesapeake's stand-alone ability to capital access analysis is based on the following principal assumptions:
  - Chesapeake remains a non-stock corporation, limiting capital access to the debt markets only (*i.e.* Chesapeake does not convert to a for-stock corporation and issue publicly traded equity securities)
  - Chesapeake intends to preserve its investment grade profile
  - Debt can be issued at the operating company level (*i.e.* GHMSI, BCBSDE and CFMD) based on the credit of Chesapeake's operating entities
- Based on these assumptions, DLJ believes that Chesapeake would be unable to fund approximately $354–$594 million of its budgeted capital expenditures

2000–2003 CapEx Requirements			2000–2003 Incremental Free Cash Flow		Capital Sources: Cash Flow		Incremental Debt Capacity		Additional Funding Needs
eCommerce	$30–$50								
New Products	170–250								
Information Management	80–120		Change in Cash		$323				
Mergers	800–900	→	Less: Required Capital	(1)	(112)	→	$375	→	$354 - $594
Total	1,080–1,320		Incremental Free Cash		$211				
Less: Forecast CapEx	(140)								
Incremental CapEx	$940–$1,180								

(1) Equals 10.0% of total change in Cost of Health Care from 1999 to 2003.

OCC 015088

ARE THERE OTHER PROBLEMS WITH DEBT CAPITAL?

In addition to Chesapeake's inability to access sufficient debt to fund its future capital needs, there are several other critical factors which argue against raising capital internally.

- Even if Chesapeake could raise $375 million of external debt financing, it would fall short of its capital needs by approximately $350-$600 million
- It would be imprudent to overborrow near the possible peak of the managed care cycle
  - No additional borrowing capacity to fund potential losses if pricing and cost trends become unfavorable
  - Inability to stave off large, deep-pocketed managed care plans looking to buy market share during period of market distress
  - High financial leverage puts Chesapeake one or two significant events away from "junk bond" status
  - Limited ability to move capital among operating companies may prevent putting capital where its is most needed
  - In the face of a market downturn and losses at the plan level, regulators may restrict ability to upstream cash from plan level to operating company to service debt, regardless of the level of excess surplus at the plans
- It would be difficult to borrow capital in the current market environment given investors' general concerns about the managed care industry
- The debt markets are fickle and there is no guarantee that Chesapeake will be able to access capital when it is most needed

OCC 015089

WHY NOT UNDERTAKE ANOTHER STRATEGIC AFFILIATION?

While another strategic affiliation may help address some of Chesapeake's capital needs, it fails to address many of the Company's broader strategic issues.

- Complicated governance and management structure becomes increasingly unwieldy as the number of affiliations increases
- Strategic affiliation opportunities are limited
- Best strategic partner (Trigon) is not an affiliate candidate
- Limited opportunity to achieve operational synergies typical in a mergers and acquisitions transactions
- Need to satisfy an increasing number of regulatory bodies
- Regulatory limitations on capital movements among entities
- Difficult to unwind or restructure in future

OCC 015090

WHY NOT UNDERTAKE ANOTHER STRATEGIC AFFILIATION? (CONT'D)

Without a detailed analysis of a potential affiliation structure, it is difficult to estimate how much incremental capital could be accessed through such an agreement. However, our preliminary analysis suggests enough borrowing capacity to meet Chesapeake's strategic needs. Nevertheless, this does not consider the capital needs of the strategic partner.

	Affiliate			
	Highmark	BCBSNC	Trigon(1)	IBC
Pro Forma:				
Maximum Debt Capacity	$800	$650	$675	$575
Chesapeake Debt	(31)	(31)	(31)	(31)
Target Debt	(250)	0	0	(10)
Incremental Debt Capacity	519	619	644	484
Incremental Chesapeake Free Cash	211	211	211	211
Cash Available for CapEx	$730	$829	$854	$695
Chesapeake CapEx:				
eCommerce	$30 - $50	$30 - $50	$30 - $50	$30 - $50
New Products	170 - 250	170 - 250	170 - 250	170 - 250
Information Management	80 - 120	80 - 120	80 - 120	80 - 120
Total	280 - 420	280 - 420	280 - 420	280 - 420
Less: Forecast CapEx	(140)	(140)	(140)	(140)
Incremental CapEx	$140 - $280	$140 - $280	$140 - $280	$140 - $280
Excess Funding Capacity	**$590 - $450**	**$689 - $549**	**$714 - $574**	**$555 - $415**

→ EXCLUDES INCREMENTAL CASH FLOW AND CAPEX REQUIREMENTS OF AFFILIATE ←

(1) While Trigon has the potential to raise capital in the public equity markets, it is an unlikely affiliation candidate due to its public ownership structure.

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