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CVS.N - Q2 2020 CVS Health Corp Earnings Call

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OVERVIEW:

Co. reported 2Q20 consolidated total revenue of $65.3b and adjusted EPS of $2.64. Expects full-year 2020 adjusted EPS to be $7.14-7.27.

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PRESENTATION

Operator

Ladies and gentlemen, good morning, and welcome to the CVS Health Second Quarter 2020 Earnings Conference Call. (Operator Instructions) As a reminder, today's conference is being recorded.

I would now like to turn the call over to Valerie Haertel, Senior Vice President of Investor Relations for CVS Health. Please go ahead.

Valerie C. Haertel - *CVS Health Corporation - SVP of IR*

Thank you, and good morning, everyone. Welcome to the CVS Health Second Quarter 2020 Earnings Call. I am joined this morning by Larry Merlo, President and CEO; and Eva Boratto, Executive Vice President and CFO. Following our prepared remarks, we'll host a question-and-answer session that will include Jon Roberts, Executive Vice President and Chief Operating Officer; Karen Lynch, Executive Vice President and President of Aetna; and Alan Lotvin, Executive Vice President and President of Caremark. (Operator Instructions) In addition to this call, our press release and Form 10-Q, we have posted a slide presentation to our website.

Please note that during this call, we will make certain forward-looking statements that reflect our current views, including our financial projections and statements related to our future financial performance, future events, industry and market conditions and the future impact of COVID-19 on our enterprise. Our forward-looking statements are based on management's estimates, assumptions and projections and are subject to significant uncertainties and other factors, many of which are beyond CVS Health's control, including the future impact of COVID-19 on our enterprise. We strongly encourage you to review the information we file with the SEC regarding these risks and uncertainties, in particular, those that are described in the Risk Factors section of our 2019 annual report on Form 10-K and the cautionary statement concerning forward-looking statements and risk factor disclosures in our quarterly report on Form 10-Q. You should also review the section entitled Cautionary Statement Concerning Forward-Looking Statements in this morning's earnings press release.

During this call, we will use non-GAAP financial measures when talking about the company's performance and financial condition. In accordance with SEC regulations, you can find a reconciliation of these non-GAAP measures to the most directly comparable GAAP measures in this morning's earnings release and the reconciliation document posted on the Investor Relations portion of our website. And as always, today's call is being broadcast on our website where it will be archived for 1 year.

Now I'll turn the call over to Larry.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

Thanks, Valerie. Good morning, everyone, and thank you for joining our second quarter earnings call. I don't have to tell you that this past quarter is unparalleled and unprecedented as we navigate the health, social and economic impacts of COVID-19. Having said that, our earnings in this environment demonstrate the strength in our strategy and the power of our diversified business model.

The environment surrounding COVID-19 is accelerating our transformation, and it's providing new opportunities to demonstrate the power of our integrated offerings and the ability to deliver care to the consumer in the community, in the home and in the palm of their hand. The pandemic has made it a necessity to contribute in ways that have called on the capabilities, expertise and footprint of many of our assets in combination to rapidly deliver solutions at scale that meet client and consumer needs and preferences.

Now those of you who have been following us for some time know that CVS Health is much more than just your corner drugstore. And in this era of COVID, our strategy of diverse assets across health care, this triad of care where connections are delivered in the community, at home and in the palm of your hand could not be more important. We have substantially expanded our community reach, which has proven to demonstrate the value of bringing differentiated assets and delivery mechanisms to bear, meeting consumer needs in delivering lower-cost, high-value care and nationwide testing, which we'll talk about in depth in just a moment.

Increasingly, the power of our assets is taking us into areas that provide greater choice as well as new areas for growth, ranging from diagnostic testing to B2B solutions, to the potential of clinical trial recruitment and enrollment. The results we share with you today underscore that our strategy is right, that it's working and that COVID-19 is driving us to bend our innovation curve markedly and accelerate solutions that will have long-term sustainability. There are numerous interdependencies in our 3 core businesses that the pandemic has made more apparent, driving the strength in our diversification while bringing new solutions to market.

So with that, let me summarize our second quarter results and the proactive steps we have taken in light of the pandemic as our team has shown great flexibility and responsiveness, adapting quickly to our clients' and consumers' evolving needs.

For the second quarter, adjusted earnings per share increased to $2.64 with total revenues of $65.3 billion. Our consolidated enterprise core performance was in line with our expectations, and our results reflect the varying impacts of COVID-19 across our business. The Health Care Benefits segment saw a positive impact from significantly lower medical costs, which was partially offset by lower volume and higher COVID-19-related expenses in our Retail/Long-Term Care segment. The COVID-19 impact in the Pharmacy Services segment was modest. Now we are raising our full year 2020 guidance to $7.14 to $7.27, and Eva will provide additional details in her remarks.

In response to the pandemic, we accelerated a number of aspects of our strategy. And our strong foundation of clinical expertise, data analytics and digital capabilities, coupled with our unmatched consumer and community reach, enabled us to rapidly address shifts in the consumer and health care landscapes. For example, our ability to quickly expand our diagnostic testing and virtual care services to meet increased customer demand highlights our ability to deliver care wherever our customers want to receive it. And we are investing in areas where we see the greatest demand and opportunity for us to differentiate our offerings across this triad of care. And we are pleased with how our new offerings are resonating with our customers, including commercial and government health plan sponsors and consumers in the thousands of local communities that we serve.

So let me transition to discussing the work we have performed within those communities. We continue to play a key role in addressing the critical need to expand COVID testing. We now operate community testing sites at over 1,800 CVS drive-thru locations, utilizing swab-and-send diagnostics. Importantly, over 50% of these locations are in communities with significant need for support according to the CDC Social Vulnerability Index.

We recently launched our Return Ready COVID-19 testing solution to our Aetna and Caremark clients. Return Ready is a fully configurable end-to-end program that enables organizations to screen and test their employees or students and monitor their populations through integrated reporting capabilities. We have over 40 clients currently enrolled, including universities and corporations across a variety of sectors and a strong pipeline of demand of over 1,000 prospects for the core testing offering as well as add-on health and safety solutions, such as contact tracing and on-site immunization clinics for the upcoming seasonal flu.

We also launched diagnostic testing for seniors in long-term care facilities. Testing and treatment of seniors in nursing homes continues to be critically important in protecting one of our most vulnerable populations. And for both Return Ready and long-term care testing, we are using point-of-care rapid test diagnostics. Through the end of July, we administered approximately 2 million COVID-19 tests, with the vast majority scheduled digitally as a result of our highly adaptable, consumer-centric digital health strategy.

And finally, we recently launched a new digital platform to assist with registering COVID-19 patients for clinical trials as vaccines and therapeutic treatments are developed. We view this new service as a natural extension of our clinical and data and analytics capabilities. Now these new diagnostic and digital services will provide sustainable value for our enterprise. As an example, 40% of those being tested at a CVS Pharmacy were not pharmacy customers previously. We're now connected with them digitally with the objective of making them long-term CVS customers. And as we look ahead, we are well positioned to administer COVID-19 vaccines once they become available through our community presence as well as on-site with our Return Ready and long-term care solutions.

Now in addition to COVID-19 testing, we continue to evolve our HealthHUB footprint and offerings. We paused HealthHUB conversions in late March, we resumed in mid-June and now have 205 locations open across 22 states. And we remain on track to open approximately 1,500 hubs by the end of 2021. Our HealthHUBs continue to perform favorably to the control group. In some encouraging metrics, it include a 15% increase in visits associated with chronic services and Aetna member visits over-indexing relative to our membership. This is an important validation point of our ability to impact medical costs through our consumer-facing assets.

Now I would note that the absolute performance in the quarter was impacted as shelter-in-place orders took effect. That said, we continue to work with clients and providers who remain interested as we develop integrated product offerings, including virtual strategies. Our work also continues in developing our Next Best Action programs, including utilizing our Pharmacist Panel capabilities. As an example, we are launching Health Advisor to Caremark clients as a new service offering in 2021.

We are enhancing our experiences from Aetna's Next Best Action program, coupled with our pharmacy panel capabilities to provide chronic disease management services designed to deliver lower medical costs and improve health outcomes. And based on test data, we are confident that significant savings will result for our customers. The pilot results reflect a 12% reduction in unnecessary ER visits along with an 8% reduction in out-of-network and non-preferred provider utilization. So this can be a real differentiator for Caremark with its clients.

This quarter, Q3, we are launching our next-generation Diabetes Management program. We're going to start with 2 large Aetna Group Medicare clients as early adopters with a broader rollout to Caremark and Aetna self-insured clients in 2021. Now in addition to the remote monitoring capabilities we currently offer through connected glucometers, this next-generation program features 3 main enhancements: interventions across more clinical categories, individualized care at the member level and member-level interventions conducted across our various channels, including our HealthHUBs and CVS Pharmacy locations, all for a reduced cost.

And finally, Transform Oncology is another new program taking advantage of enterprise assets. Our oncology spending is projected to exceed $240 billion by 2023, growing at a CAGR of about 10%. So helping clients address this important area will be a critical market differentiator as we move forward. To date, the program has engaged about 70 provider systems with approximately 20% of Aetna's insured eligible oncology population enrolled. And while enrollment slowed during COVID, we are encouraged by the early adoption, and we will continue to scale as oncologist practices return to normal. Medical cost savings will vary across patient type, and this is clearly an important area of focus given our commitment to lower customer cost trends.

Now let me move to providing care at home because we continue to experience high demand for our home health and delivery services. Our retail prescription home delivery volume is up more than 500% in Q2 versus Q1 of this year, and we continue to focus on increasing our front store attachment rate. In addition, our specialty pharmacy capabilities where we have driven continued growth include our Coram infusion professionals who have now conducted more than 160,000 home visits year-to-date, collaborating with hospitals and providers to help transition eligible IV therapy patients to home-based care. This frees up important hospital bed capacity while reducing the cost of care. And as an example, we see medical cost savings of more than 50% for patients who are receiving infusions at home versus in an outpatient setting. So by focusing our service delivery on the most cost-effective channel, we are able to make care more affordable for our payers and their members.

And moving to delivering care in the hand. As you would expect, we saw continued demand for virtual care and increased digital engagement, and we continue to expand our virtual care offerings. This includes providing access to care for our Aetna-insured members through MinuteClinic video visits and through our own newly launched virtual care program called E-Clinic, which is staffed by MinuteClinic providers. Our virtual care offerings target a variety of health care needs, including diagnosis in the treatment of common injuries, behavioral health and the management of chronic conditions. And our total MinuteClinic virtual care visits are up over 750% compared to Q2 of last year.

So in conclusion, we continue to make significant progress on our strategic priorities, including the delivery of our integration synergies. And our diversified, resilient and innovation-driven business model, combined with our strong cash position, has enabled us to accelerate many aspects of our plan to meet consumer demand. And our integrated model is resonating with clients and consumers, and we are seeing tangible evidence of value creation. And we expect the momentum we've generated to continue to drive value for our clients, consumers and shareholders.

So with that, let me turn the call over to Eva.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Thanks, Larry, and good morning, everyone. Echoing Larry, these are certainly unprecedented times for all. We have been on the frontline supporting our local communities while continuing to advance our key strategic priorities, including product and service innovation, the delivery of integration synergies and cost-savings initiatives.

Looking at our second quarter performance, the diversity of our portfolio of assets enabled our enterprise to exceed our expectations. During the quarter, we generated $7.1 billion of cash from operations, reflecting the underlying performance as well as the impact of the deferral of certain tax payments in connection with COVID-19-related extensions of payment deadlines. In July, we repaid $2.75 billion of scheduled debt principal, and we remain committed to achieving our low 3x target leverage ratio in 2022. We also returned approximately $660 million to shareholders through cash dividends.

In the third quarter, we completed the sale of our Workers Compensation business for $850 million in gross proceeds in our Health Care Benefits segment. This divestiture is expected to be about a $0.02 drag on adjusted EPS in the remainder of 2020, which is included in the guidance we have provided this morning. As I've said previously, we remain laser-focused on delivering long-term value. In support of that focus, we are continuing to evaluate and assess all aspects of the enterprise to identify areas that may not be consistent with our long-term strategic priorities.

Moving to the P&L. Consolidated revenues of $65.3 billion increased 3% year-over-year with growth primarily coming from the Health Care Benefits and Retail/Long-Term Care segments. Adjusted EPS grew to $2.64 with the majority of our growth attributable to the Health Care Benefits segment, which saw an unprecedented decline in utilization due to the pandemic. Our Retail/Long-Term Care segment was affected by substantial investments made in our stores, colleagues and consumers, a reduction in new therapy prescriptions due to lower provider visits and reduced front store traffic. The Pharmacy Services segment continues to execute and deliver underlying core growth in the quarter. The total favorable impact of COVID-19 on our second quarter results is estimated to be $0.70 to $0.80.

Let's turn to operating results by segment. In our Health Care Benefits segment, total revenues increased 6.1% year-over-year, primarily driven by membership growth in our government products. Adjusted operating income increased substantially, reflecting an unprecedented MBR of 70.3%, primarily driven by a reduction in benefits costs related to the deferral of elective procedures and other discretionary utilization. The results include investments made in our customers and members and provisions for potential payments to clients and plan sponsors for contractual and regulatory requirements as well as support for our providers. The total quarter impact of COVID-19 on HCB operating income is estimated to be in the range of $1.8 billion to $2.1 billion.

Our medical membership grew by 124,000 lives sequentially, driven by the continued strength of our government products, partially offset by a decline in our commercial products. We are extremely pleased with the continued success of Medicare Advantage, which grew membership 2.6% sequentially. Growing Medicare Advantage is one of our key strategic priorities. We believe that our integrated assets, which enabled differentiated client service capabilities, will continue to support our high Star Ratings, giving us competitive advantages and resulting in our ability to continue to win new members in this space.

Additionally, in Medicare Part D, we are pleased with the preliminary benchmark results received from CMS for the 2021 plan year where we qualified in 33 of 34 regions. This is an important enabler of our overall Medicare growth strategy. Our Medicaid membership grew 4.9% sequentially as states responded to the COVID-19 pandemic by suspending eligibility redeterminations, and we saw some uptick due to increases in unemployment. We continue to view Medicaid as a focus area with a strong pipeline of opportunities headed into 2021.

Commercial membership declined approximately 0.5% sequentially, reflecting the impact of unemployment. As we have mentioned previously, our employer-sponsored portfolio is diversified and does not have a significant concentration in any one industry or geography.

Days claims payable were 57 days for Q2, reflecting the depressed utilization we saw largely in April and May as a result of shelter-in-place orders from COVID-19. A significant portion of the quarter-end medical claims liability includes June dates of service where utilization was near normalized levels. We expect days claims payable to decline as utilization returns to more normal levels.

Within Pharmacy Services, total revenues were essentially flat year-over-year as growth in specialty pharmacy and brand inflation were largely offset by the previously disclosed client losses and continued price compression. Caremark customers continue to recognize CVS Health as a leader in specialty medication cost and utilization management. As a result, second quarter specialty pharmacy revenues increased approximately 15% year-over-year, reflecting new client and existing channel growth.

Pharmacy Services adjusted operating income increased 2.4%, and gross margins improved slightly versus last year. Overall, COVID-19 unfavorably affected operating income by approximately $50 million, reflecting lower new therapy starts and higher operating costs. PBM performance reflects the growth in specialty I mentioned previously and continued improvement in purchasing economics. Our scale and expertise, including benefits from Red Oak and our ability to negotiate with manufacturers, enable us to deliver optimal value to our clients and CVS Health.

Our Pharmacy Services membership remains in line with expectations as reductions in commercial were more than offset by increases in Medicaid, given our strong position in the marketplace. Additionally, to further assist our clients, in the second quarter, CVS Health launched Zinc Health Services, allowing us to deliver new, innovative ways to further reduce the cost of brands and specialty drugs. This new entity will be responsible for certain negotiations with manufacturers, but will not make any formulary decisions. While we have continuously worked with industry pharmaceutical manufacturing leaders to lower cost and deliver greater savings, this new approach will give us even greater flexibility and agility to continue in those efforts. This approach will ultimately help make medications more affordable for our clients and members.

Shifting to the Pharmacy Services 2021 selling season, our renewals are now approximately 90% complete with a strong 98% retention rate. To date, we have won $4.3 billion in gross new business for 2021, and we continue to increase our pharmacy penetration within the Aetna book of business with approximately $250 million in incremental revenue. We are very pleased with these results.

Moving to Retail/Long-Term Care, COVID-19 continue to have a significant impact on this segment's performance in the quarter. Despite the challenging environment, total revenues grew 1% year-over-year. Growth was dampened by lower prescription and front store volume due to lower provider visits and stay-at-home orders in Q2. Front store revenue declined due to reduced store traffic, partially offset by an increase in basket size. As the quarter progressed, we saw improvements in sales as store traffic began to return as states relaxed their stay-at-home orders.

Gross margins for the segment declined 240 basis points versus 2019. Nearly half of the decline was attributable to purchasing patterns in the front store as well as drug mix, largely as a result of COVID-19. Also contributing to the decline was the ongoing pharmacy reimbursement pressure. Front store margins were relatively consistent with prior year.

In the quarter, this segment incurred approximately $240 million in COVID-related investments due to colleague benefits, providing free home delivery to help keep patients stay on their medications, providing protective equipment and enhanced cleaning to keep both our colleagues and consumers safe. Overall, we estimate the impact of COVID to Retail/Long-Term Care results in Q2 of approximately $525 million to $575 million.

Going below the line, our interest expense was $765 million, and the adjusted effective tax rate was 24.5% for Q2. The lower tax rate contributed about $0.10 to Q2 earnings, reflecting the favorable resolution of several state and local income tax matters.

Given the highly unusual and fluid environment in which we are continuing to operate, let me quickly provide an update on some key metrics, including July. Within the Pharmacy Services and Retail/Long-Term Care segments, we saw prescription volume growth accelerate in June as members refilled 90-day prescriptions from March. In June, front store growth started to benefit from states reopening, followed by customers stocking up on key preventative and treatment items in the Sun Belt states during July. In Health Care Benefits, medical cost utilization largely returned back to normal levels in June and July, but obviously varies by geography and lines of business.

Moving to guidance. While acknowledging the inherent and unprecedented uncertainty surrounding COVID-19 and its impact on us, we are raising our full year adjusted EPS guidance to $7.14 to $7.27 to reflect the favorability in the tax rate we experienced in the quarter. In addition, we are increasing our full year 2020 cash flow guidance to $11 billion to $11.5 billion, reflecting the timing of the payments of certain liabilities. Though our cash from operations reached $10.4 billion through the first 6 months of 2020, we expect higher payments in the second half of the year. Those payments include, among others, projected increase in medical costs, costs related to COVID-19, the 2020 HIF and the estimated income tax payments normally due in the second quarter that were extended to July. We remain committed to reducing our debt as initially planned, and we are on track to meet our deleveraging target of low 3x in 2022.

Let me provide additional commentary by segment and on the cadence of our adjusted earnings per share guidance. We expect approximately $2 billion of COVID-19-related investments for the year, of which about 40% was incurred in Q2. Approximately $1.5 billion of the $2 billion will impact HCB, benefiting customers, members, including premium credits, minimum MLR rebates and contractual requirements. About 35% was reflected in HCB's Q2 results. For Retail/Long-Term Care, we expect approximately $400 million of investments with $240 million reflected in Q2. Clearly, the timing of these investments will affect the earnings cadence for the back half of the year.

Furthermore, in our Health Care Benefits segment, we expect membership to be affected by unemployment as well as the loss of a large public and labor ASC customer effective September 1. We also expect to continue to see increases in Medicaid membership as a result of the current economic environment. We expect utilization in the back half of the year to remain at more normal levels with select geographies continuing to be affected by COVID-19 waves. In addition, we expect higher costs related to COVID-19 testing and treatment.

Turning to the Pharmacy Services segment, we expect the business to continue to deliver growth in the second half of the year, reflecting strong specialty performance, the continued strength of our assets, position in the industry and continued execution of our strategy.

And finally, in Retail/Long-Term Care, we expect the back part of the year to be affected by the COVID-19 G&A expenses and to benefit from our testing capabilities. Additionally, we expect gross margins in the second half of the year in line with our year-to-date results, improving from our second quarter performance. We remain confident in delivering $800 million to $900 million in integration synergies, and our cost-savings initiatives remain on track to deliver $450 million to $550 million.

In summary, our financial resilience through this period reflects the effects of successful integration of our enterprise. Our ability to deliver results in this dynamic environment is evidence of the strength of our diversified model. We are continuing to make progress on our strategic plan to deliver new products and services, all while making health care more affordable and accessible. Our continued execution and strong cash generation are propelling us toward achieving our long-term sustainable growth.

With that, let's open it up for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We'll take our first question from George Hill with Deutsche Bank.

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

I guess, Larry, the COVID crisis has kind of reshaped the care delivery model pretty dramatically in the last 3 to 4 months. You've talked about how it's impacted the HealthHUB strategy. I guess, can you talk a little bit about how you think about through the Aetna business kind of engaging the care delivery model? And does it change how you think about the white space in what you want to own and what you don't want to own? And Eva alluded to that a little bit in kind of the portfolio process, but I would just love to hear how the COVID crisis is changing how you think about the delivery model and what pieces you want to own.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

Yes. George, thanks for the question. And George, maybe I'll start with I think all of what we're seeing is, I'll call it, the acceleration of omnichannel for health. And I would describe that as speaking to care being delivered in multiple and nontraditional settings. And I think we're going to see a new value proposition emerge that is going to be based on the elements of convenience, cost, quality and trust.

So George, I would say, direct to your question, obviously, there's a technology component of that. And you heard in our prepared remarks, care in the community, in the home, in the palm of your hand, obviously, that speaks to what we've seen around the acceleration of virtual care of telemedicine. And I think it opens up the door for a greater acceptance of remote monitoring through technology, and that speaks to care from the comfort of your home.

Then there's care in the community. And think about what we talked about this morning around testing, the broader opportunity that, that creates with diagnostics, vaccines, immunizations, you start thinking about the role of the pharmacist, the nurse practitioner. And what we have seen over the last several months, with regulations being relaxed, it has allowed them to perform to a higher level to the top of their license. So you start thinking about why go backwards when it's more convenient, less costly and administered by someone that they know and trust. And look, it also speaks to why retail does matter and the importance of our strategy of pivoting our retail asset and offering more health services at retail.

And then, George, just related to that, it's a little indirect to your question, but I think we see some of the other changes on the horizon as we've got to have a more integrated approach to behavioral and physical health. And we're seeing way too many examples of people feeling the stress, the anxiety of everything going on. And this is an area of health that cannot be ignored, and we have to do better. And finally, George, we've talked a lot over the last several years about payment reform, value-based care. We see the challenges that providers are experiencing economically and will the pandemic be the spark that really accelerates more rapid growth of value-based reimbursement in care.

Operator

We'll take our next question from Michael Cherny with Bank of America.

Michael Aaron Cherny - *BofA Merrill Lynch, Research Division - Director*

I wanted to ask a question on the retail side. Clearly, there's a lot of moving pieces in this specific quarter. Actually, normal, I think, wouldn't do the term justice. As you think about the incremental investments that you're making now, how much of the new procedures, new cleaning process, staffing dynamics that you have in place are the type of investments that might continue on a long-term basis? And how does that factor into the thought process and framework you had about where Retail, in particular, should grow into 2021 and beyond?

Jonathan C. Roberts - *CVS Health Corporation - Executive VP & COO*

Yes, Mike, this is Jon. So we do expect these enhanced cleaning procedures to continue for the foreseeable future, and I think that's until we get a vaccine and COVID essentially goes away. As Larry said, we're making a significant pivot to health care services, whether it be the COVID testing we're doing, we're gearing up for a pretty significant flu vaccine season, and the repositioning of our retail footprint and the HealthHUBs supports that health care services move. So we view it as evolving to higher-margin health care services as we move forward.

Operator

We'll take our next question from Ricky Goldwasser with Morgan Stanley.

Rivka Regina Goldwasser - *Morgan Stanley, Research Division - MD*

Thank you for the comment on the testing and the vaccine. I just wanted to dig a little deeper into them. Can you give us a little bit of color on the revenue model that's associated with the testing, the turnaround time that you're seeing? And then on the vaccine side, when you talk about first in the flu -- early flu season, are you -- what type of magnitude are you expecting to see in terms of demand for flu vaccine? And if you can just share more on your role on the COVID-19 vaccine administration and what conversations you're having with manufacturers. We're getting a lot of questions from investors on the setting for vaccine administration. So I'd love to get your insights on that.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

Yes, Ricky, it's Larry. And Ricky, I'll start and then ask -- flip it over to Eva to take the economic side of your question. And yes, Ricky, maybe I'll start with the seasonal flu. And look, we expect to administer up to 18 million seasonal flu vaccines this fall, which is more than what we have administered in the last few years. We think that, for obvious reasons, there's going to be an increased demand. You're going to see a lot of PSAs out there largely sponsored by the government at both the federal and state level. And Ricky, when you think about it, the symptoms of the seasonal flu mimic the symptoms of COVID. And the importance of the seasonal flu vaccine is never going to be more important this year than any other prior year because we've got to try to separate that dynamic in terms of what are we talking about.

If I shift, Ricky, to the vaccine, we are having discussions with the administration in terms of the role that we can play, and there's absolutely an important role for us to play. And Ricky, some of this goes back -- I'll go back 10 years or 10-plus years with H1N1 that pharmacy became the local solution to administer vaccines to millions of Americans across the country. That is not lost on the administration.

And Ricky, I think what is unique for us is this is where the intersection of testing and vaccine creates a sustainable business model because I couldn't be prouder of the work of our CVS colleagues in standing up the testing business in 1,800 drive-thru locations in a matter of a few weeks. And we've also used our digital capabilities, as you heard in our prepared remarks, where customers can actually schedule -- are required to schedule an appointment to get the test. But you don't see 6, 8 hours of cars backed up trying to get a test in one of our drive-thru sites. And we can bring that same digital and technology capability to scheduling vaccines when they become available. So I think we're in a great place there to be an important part of the solution.

And I'll flip it over to Eva on the testing economics.

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Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Yes. Ricky, I would say, overall, as you think about testing and our economics, think about it in the margin range of diagnostics and typical testing.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

And Ricky, I think you had a question in there in terms of what the country has experienced around testing turnaround times, and I'll just quickly hit on that. As you heard in our prepared remarks, we've administered about 2 million tests to date. The turnaround times through the months of May and June were in that 3-day range. And coming out of the July 4 holiday, we did see a spike in testing demand as well as a spike in the turnaround time.

We took immediate actions. The first thing we did was actually reduce the number of tests we were doing on a daily basis by 25% in working with the labs as they were working to increase their capacity. We've also added 2 additional labs to our testing back office, if you will, okay, where they're producing the results. And as we said today, we have seen a dramatic improvement from where we were coming out of that July holiday. There's still some additional improvement that needs to be made by one of the labs, okay?

And at the same time, Ricky, we talked about our Return Ready testing with our B2B clients. We're utilizing, as you heard in our remarks, the point-of-care testing diagnostics. And we're also working to pivot some of our retail sites to more point-of-care testing, and we're currently working with the administration in terms of creating the reimbursement codes that don't exist today for that type of retail testing. So I think that's going to be important. As a country, we're testing about 17 million people a month. If you look at the experts, they're saying there's going to be an increased need in the fall time frame of the 26 million to 28 million tests per month range. And more point-of-care testing is going to be an important part of that solution.

Operator

Our next question is from Eric Percher with Nephron Research.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

Eric Percher and Josh Raskin here. Can you quantify some of the impact of the $1.5 billion in investment for COVID in HCB? And I guess, specifically, I'd be interested in mandatory rebates on items like that versus voluntary investment.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Eric, it's Eva, and I'll take that question. First, let me define what's in that investment at the company level. Overall, as we look at the investments, $2 billion at the company level, $1.5 billion for the year at HCB, these are items that are going to affect our earnings, right? So essentially, they include operating expenses, refunds, rebates and credits to support our customers, members and clients. What I would say, we're not breaking out each of those individually, but all of those are contributing to the underlying $1.5 billion in HCB.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

Okay. And then just to follow up on something you mentioned, Zinc Health. Could you tell us what that is? And are you partnering with others? And are there any tax benefits there?

Alan M. Lotvin - *CVS Health Corporation - Executive VP & President of CVS Caremark*

Well, I'll start. This is Alan Lotvin. I'll start with what Zinc is, and then I'll let Eva talk about the tax question. So Zinc is an onshore entity that we created to essentially develop and extract more value out of the pharmaceutical manufacturers on behalf of our customers and clients as part of the purchasing economics that Eva has referenced a couple of times.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

And Eric, just to perhaps state the obvious, as Alan said, it's onshore. We did not design Zinc as a tax strategy. It's around the value that we can deliver from a business perspective to our customers and CVS.

Operator

Our next question is from Justin Lake, Wolfe Research.

Justin Lake - *Wolfe Research, LLC - MD & Senior Healthcare Services Analyst*

I wanted to follow up -- a lot of moving parts for 2020, obviously. So just wanted to get your view on kind of what the right kind of jumpoff number is for 2020 earnings and kind of some of the moving parts in your mind. And then thinking out to 2021, I'm going back to Michael's question on kind of the potential run rate costs in the Retail business, for instance, you talked about a mid-single-digit EPS growth rate. Is that still kind of -- is that still the company's view just given everything going on? Any kind of color there would be helpful as well.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Justin, thanks for the question. In terms of the right jumpoff, what I would say is the reason we provided all of the transparency around the COVID-related effects was to help the investment community really understand outside of COVID how the businesses are performing. I think if you look at how we've performed at the enterprise level through the first half of the year, normalizing for COVID, right, we've been performing in line with our expectations. And there's nothing around our underlying fundamentals that have taken us off our strategy and trajectory.

Justin Lake - *Wolfe Research, LLC - MD & Senior Healthcare Services Analyst*

So that would indicate that the strategy trajectory is the same, so the 2021 trajectory would be similar as well versus previous?

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Yes, there's -- as I said, underlying, you got to think about how COVID is affecting, but our underlying core is in line with our expectations when we started the year. And we'll continue to work towards delivering on what we outlined at our Investor Day.

Operator

We'll take our next question from Bob Jones with Goldman Sachs.

Robert Patrick Jones - *Goldman Sachs Group, Inc., Research Division - VP*

I guess maybe just to follow up on that last question from Justin. I mean I know it's got to be extremely difficult to parse out what's exactly COVID-related versus what is not. But it does look like in the Retail business, even excluding the amount that you highlighted, that margins are still down a few hundred basis points year-over-year. Is there anything else you could parse out as far as what you're seeing from mix dynamics and maybe other areas, traditional areas like procurement? Anything around cost there? And then just how you're thinking about those factors as we think about your expectation, Eva, for gross margins to be in line in the second half with the year-to-date results?

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Yes. Thanks for the question. So in terms of gross margin, let me go back a bit, in the segment, margins declined about 240 basis points, as I said on my prepared remarks. About half of that, nearly half of that was what I'll call mix. So as you look at the purchasing patterns with pharmacy growing faster than front in the quarter, given the disruption by COVID, there's an impact there as well as mix within the underlying front store basket as sales were lower in the consumer health and beauty categories, which carry a higher margin. And we also saw some drug mix impacts with new prescriptions depressed and the effects on the generic dispensing rate.

I think if you look year-to-date at how Retail/Long-Term Care is performing, it's performing well when you normalize for all of the different factors. Obviously, margins were stronger in the first quarter, and we do expect them to improve in the back part of the year.

Robert Patrick Jones - *Goldman Sachs Group, Inc., Research Division - VP*

That's helpful. And then, Larry, if I could just follow up, I thought it was really interesting, some of your comments on the care from the comfort of your home, and you talked about the new diabetes management program. I was wondering if maybe you could expand on that a little bit, just what the new diabetes program looks like relative to the previous one. And then just any other comments on your digital solutions that you're developing as you think about the evolving landscape in some of these more differentiated offerings that you're bringing to the market.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

Yes, Bob. And maybe just one other point, just back on Eva's -- your question on Retail. The other thing to keep in mind is we shut off a lot of our ExtraCare programs as we went through the shelter-in-place orders. So those have been turned back on, and that's another contributing factor in terms of why we would see a more normalized margin trajectory in the second half of the year.

And then, Bob, moving on to your question on the diabetes programs. A lot of it, Bob, is tied to managing the consumer, if you will, in a more holistic fashion. So today, we remotely manage their blood glucose levels with connected glucometers as one example. But we believe there's a much more broader opportunity, recognizing it's just not about managing the diabetes condition. It's also managing the comorbidities that are associated with that, okay, that go beyond diabetes as a chronic disease. And those are things that we're going to be focused on that we believe, at the end of the day, are some of the real drivers in terms of bending the cost curve for those individuals and what we've seen with the pilot programs that we've done.

Operator

We'll take our next question from Steven Valiquette with Barclays.

Steven James Valiquette - *Barclays Bank PLC, Research Division - Research Analyst*

I guess with the commercial membership down only about 2% year-over-year in the second quarter, I guess I was curious to hear more about how that stacked up versus your expectations. And then are there any broad goalpost you can put around your commercial membership assumptions that are built into the guidance for the back half of 2020?

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Karen Sue Lynch - *CVS Health Corporation - Executive VP & President of the Aetna*

Steve, it's Karen. Relative to commercial, we had anticipated more losses in commercial than we saw in the second quarter. We do think that's related to companies doing more furloughs than eliminating jobs. However, as we turn the corner for the rest of the year, we anticipate that we'll see continued commercial losses due to unemployment as the year emerges, although what we're seeing in July is similar to what we saw in each month of the second quarter. But you can anticipate lower membership for commercial for the latter half of the year.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

And Steve, obviously, in terms of what actions the government could take, that number could vary, right? There's uncertainty there.

Steven James Valiquette - *Barclays Bank PLC, Research Division - Research Analyst*

Okay. Just a quick follow-up just around Medicaid reimbursement adjustments. There's some that can happen for 2020 and then some for next year. As far as the ones for 2020, any clawbacks, et cetera? Just curious if that's something that is material within any of the guidance assumptions for you guys. Or is that just kind of rounding error within the overall company as far as the guidance assumption for 2020 in particular?

Karen Sue Lynch - *CVS Health Corporation - Executive VP & President of the Aetna*

Yes. Relative to 2020, it's rounding, and we have factored it into our -- the numbers that Eva gave you relative to that $1.5 billion. What I would tell you on Medicaid is every single state that we have has already built in mechanisms to return any additional profit. So that's all been factored in, but not material.

Alan M. Lotvin - *CVS Health Corporation - Executive VP & President of CVS Caremark*

Steven, it's Alan. The one thing I would add is we have seen a reasonably significant uptick in membership within our Medicaid lives and the PBM. So you are seeing that -- the shift and the demonstrated power of having a broadly diversified book.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

So we'll go ahead. And operator, we'll take 2 more questions. And we know that many of you have another call at 9, and we want to be respectful to that.

Operator

And we'll take our next question from Stephen Tanal with SVB Leerink.

Stephen Vartan Tanal - *SVB Leerink LLC, Research Division - MD & Senior Research Analyst*

It sounds like you may have had some pretty solid wins in the national account part on the Aetna business. So I was hoping to just follow up there. And I'm wondering how HealthHUBs may have contributed, if at all, and whether there's any self-insured clients that have made them a central part of their network design at this stage.

Karen Sue Lynch - *CVS Health Corporation - Executive VP & President of the Aetna*

Relative to national accounts, just let me give you kind of broad perspective, our national account customers are interested in our integrated value and our integrated story. What I would tell you, if you look at our 2021, we have sold 4x more pharmacy members this time compared to last year for 2021. And we've improved our pharmacy penetration from 34% to 39%. But as I -- and we also are doing a lot to be in the market relative to the HealthHUBs.

But relative to national accounts, it's been a lumpy season for us. We did see a fair amount of our customers in RFPs pull back and defer some of their decisions until 2022. We've had very solid retention. We've had some good sales. But generally speaking, if you look to 2021, I'd say that national account membership will be flat to down, really reflecting in-group attrition from unemployment. However, on the Group Medicare side, we've had very strong retention in the high 90s, very solid sales, and you can expect growth in 1/1/21 from Group Medicare.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

And Steve, maybe I'll ask Alan to comment similar question to the PBM in terms of selling season.

Alan M. Lotvin - *CVS Health Corporation - Executive VP & President of CVS Caremark*

Yes. So on the selling season, in general, we're about 90%. Through the sales season, we have a 98% retention rate. As Eva said, we have $4.3 billion in gross new wins. We haven't -- I'd say the season itself has been interesting in the lumpiness with COVID, but overall ending up about where we thought. The health -- specifically around HealthHUBs, we've seen a tremendous amount of interest in the HealthHUBs, not just from national accounts, but also from our health plan customers who want to understand how to better connect with their members in the community. So very happy with where the sales season is right now. So -- and again, as I said, a strong interest in the HealthHUBs.

Operator

And the next question comes from Lance Wilkes with Bernstein.

Lance Arthur Wilkes - *Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst*

Just a question on your comment on looking at noncore assets and potential strategies related to them. I just want to understand the performance in the Long-Term Care business, the status of the turnaround there and if there are any other assets that are particularly in focus as noncore.

Eva C. Boratto - *CVS Health Corporation - Executive VP & CFO*

Lance, it's Eva. So in -- let me take your second question first, right? I don't have any specific comments in terms of where we're -- the things we continue to evaluate. But what you've seen us do is we divested our Brazilian operation that CVS owned, now Workers Comp. And what I can tell you is we continue to just thoroughly evaluate what's in our portfolio, how the dynamics in the marketplace are changing to make sure we're optimizing the business.

In terms of Long-Term Care performance, obviously, it's been a segment that has been substantially affected by COVID, right? As you look at the industry challenges, we've seen, as an industry, admissions down about 20% and facilities -- some facilities continuing to not accept new patients, but not be shut down per se. As you look at what long-term care contributes to our overall bottom line enterprise, right, it's less than 2% of our overall enterprise profitability.

As you look at what we're doing, we have made substantial improvements related to our service model over the last 12 months. And in Q1 of this year, we had the highest customer satisfaction score since we've been tracking this back to 2015. We're also -- COVID and testing this vulnerable patient, right, we're continuing to drive opportunities there, as Larry highlighted. And I would say we are aggressively managing our cost structure in this environment. And we have new leadership leading the Long-Term Care business, and we're really focused on driving improved performance here.

Larry J. Merlo - *CVS Health Corporation - President, CEO & Director*

Okay. So with that, let me just go ahead and wrap up before we sign off here. And a big thank you and my sincere gratitude to our 300,000 colleagues for all of their hard work across all parts of our organization, especially those that are working the front lines. And they have just displayed incredible commitment and effort during these unprecedented times. And all of that represents our best in terms of our commitment in helping people on their path to better health. And we're proud to be able to serve our communities at such a crucial time in our nation's history.

So with that, thanks again for joining us this morning, and please stay safe and healthy.

Operator

And this will conclude today's CVS Health Second Quarter 2020 Earnings Call and Webcast. You may now disconnect, and have a great day.
