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CVS - Q4 2018 CVS Health Corp Earnings Call

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OVERVIEW:

CVS reported 4Q18 results. Expects 2019 revenues to be $249.9-254.3b and adjusted EPS to be $6.68-6.88. Co. also expects 1Q19 GAAP EPS to be $1.04-1.08 and adjusted EPS to be $1.49-1.53.

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Good morning, everyone, and thank you for standing by. Welcome to the conference call to discuss CVS Health's fourth quarter 2018 results and 2019 outlook. As a reminder, this call is being recorded on Wednesday, February 20, 2019.

I'm Mike McGuire, Senior Vice President of Investor Relations for CVS Health. I'm 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. (Operator Instructions)

In addition to this call and our press release, we have posted a slide presentation on our website that summarizes the information in our prepared remarks as well as some additional facts and figures regarding our operating performance and guidance. Our 10-K will be filed later this month, and that, too, will be available on our website once filed.

I have one announcement this morning. Our annual Investor Day has been scheduled for Tuesday, June 4, in New York City. You will have the opportunity to hear from our senior management team, who will provide a comprehensive update of the execution of our strategic vision and an in-depth review of our strategies for driving long-term growth and creating shareholder value. We plan to send invitations via e-mail with more specific details in the spring, but please save the date. Again, that's Tuesday, June 4.

Please note that during this call, we will make certain forward-looking statements that reflect our current views related to our future financial performance, future events and industry and market conditions and forward-looking statements related to the integration of the Aetna acquisition, including the expected consumer benefits, financial projections and synergies. These forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from what may be indicated in the forward-looking statements.

We strongly encourage you to review the information in the reports we file with the SEC regarding these specific risks and uncertainties, in particular, those that are described in the Risk Factors section of our annual report on Form 10-K and the cautionary statement disclosures in our quarterly report on Form 10-Q. You should also review the section entitled Forward-Looking Statements in our earnings press release.

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

Now I'll turn this over to Larry Merlo.

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

Thanks, Mike. Good morning, everyone, and thanks for joining us today. We achieved strong performance in the fourth quarter and in full year 2018. And importantly, with the completion of our merger with Aetna, we have positioned CVS Health to excel in a market that is undergoing profound and rapid transformation.

In recent years, it has become increasingly evident that the path to long-term growth and value creation lies in the establishment of new integrated health care models that provide consumers better care and convenience at a lower cost. And since closing the Aetna merger, we are increasingly confident in the synergistic potential of this powerful combination to build and deliver shareholder value. CVS Health is in a superior position to lead the change needed in a fragmented U.S. health care system with our compelling fully integrated health care offerings, our unmatched local community assets, proven pharmacy care leadership and a commitment to collaborating with health care providers to achieve the very best outcomes for the patients and clients we serve.

In 2018, we delivered on our financial expectations as did Aetna, laying a strong foundation for a successful combination. We generated significant cash flows with nearly $7 billion of free cash for full year '18, consistent with our expectations. And we returned $2 billion back to shareholders through dividends and later deployed the cash we raised in early '18 to fund the Aetna merger. So in short, 2018 was a milestone year both tactically and strategically as we successfully completed our transformational merger with Aetna.

Now we also delivered our key foundational steps for growth in health care services. This includes making more than 80% of primary care services available to consumers at MinuteClinic, while also increasing home visits by Coram for infusion services by more than 15%. Importantly, we began effective implementation of our integration strategy and took important steps toward building the integrated health care model that will bring substantial value to our various stakeholders.

Now we expect 2019 to be a year of transition as we integrate Aetna and focus on key pillars of our growth strategy, creating a more consumer-centric health care experience. As an example, our first 3 concept stores were unveiled earlier this month. And you probably saw the press coverage last week, and there's a lot of excitement around the consumer engagement and response. Now it's still early as we're in the learning phase and working to define a hub-and-spoke approach, but it's an example of the work underway, and I'll share additional progress on achieving our vision in just a few minutes.

Now that said, we're also fully aware of the need to address the impact of certain headwinds that are having a disproportionate impact in '19 when compared to prior years. Many of these issues we've talked about previously, and most significant is the ongoing pharmacy reimbursement pressures in our businesses and the reduction in offsets to those pressures. What we're experiencing in '19 is a declining benefit from new generics, lower brand inflation and the ongoing questions around rebates, along with some structural and CVS-specific challenges in the long-term care space. And while these factors will negatively affect the business in the short term, I want to outline the comprehensive actions we have taken in response.

In our Retail business, we are continuing to develop product and service initiatives that will accelerate top line revenue and profitability. We are winning from a growth perspective, and we expect to continue on those positive trends. In the front store, this includes introducing new product lines in the health and beauty areas, along with the expansion of higher-margin service offerings.

In the pharmacy, we will continue to deliver market-leading top line growth through our network relationships and clinical care programs. Additionally, we are developing a new retail contracting strategy that better aligns reimbursement to the value our clinical products provide, enabling adherence improvements and store enhancements while saving patients money, to name just a few.

Second in the PBM, we've created a new contracting model that provides for more transparency, simplicity for and alignment with our clients. The Guaranteed Net Cost pricing model is an innovative way to approach the market by allowing us to maximize all cost control tools at our disposal. In this model, clients will receive 100% of rebates while we leverage our core strengths of contracting expertise and utilization management to drive lower net costs for our clients and members without compromising on the quality of care.

Now this is a win-win. Clients will benefit from the simplicity of one guaranteed price per claim that's focused on lower net costs and not discounts and rebates. Now we've introduced this approach to clients and benefit consultants, and we will have a small number of clients adopting the model this year. We expect a more rapid adoption in '20 and beyond.

Third, back in August, we outlined a 4-point plan to get the Long-Term Care business back on track. And while progress is being made in the identified areas, the benefits are being offset by the external factors impacting the Skilled Nursing business. And work is underway to accelerate the action plan time line to achieve the benefits more quickly. And we've already begun to see some progress, realizing nearly $80 million in process improvement savings with more to come.

Fourth, in early January, we began planning a new cost-reduction effort across the enterprise, going beyond the previously announced productivity initiatives of the legacy companies and targeting opportunities that neither company would be able to accomplish as a stand-alone. This effort is in addition to the near-term synergy work tied to the $750 million target, which we are on track to exceed.

As we look across the new combined enterprise, there are significant streamlining opportunities in member enrollment, clients processing and customer service as well as through the use of robotics and advanced analytics. Additionally, we are focused on aggressively managing working capital, especially through the reduction of inventory and improvement of terms within our payables. And we'll have more details for you on our May earnings call.

And finally, we continue to evaluate our assets and the roles they play in enabling the core strategies of our new company. So we'll provide updates to the actions we have underway as we execute our vision in a strategic and innovative, yet practical, realistic and carefully prioritized way. We understand acutely the importance of balancing near-term execution with longer-term vision, and we are confident that these actions will position us well in 2020 and beyond.

Now several key pillars that we are executing on today will drive above-market growth going forward in this rapidly changing health care environment. And a few key initiatives that underlie the ongoing execution of our strategy are as follows.

First, we are growing membership. We are working to expand the reach of our government business with Medicare positioned to lead the way. Medicare Advantage top line growth is being driven by the addition of new membership in existing markets and continued geographic expansion. Driving excellence in STAR ratings continues to be a primary focus for our business. And by enhancing our clinical model, products and capabilities, we are expanding our offering to take care of higher-acuity and complex members, including dual-eligibles, a critically important set of beneficiaries, when bending the cost curve.

Our success in building the largest Medicare Part D plan, SilverScript, while simultaneously becoming the partner of choice for more than 40 health plan Part D clients, gives us the confidence that we can further expand upon the success of both organizations. Looking ahead, we see a strong and growing pipeline of new business opportunity within Group Medicare for 2020. And we see opportunity as well within Medicaid, building upon the success we've had with recent wins in Kansas and Florida. And of course, we are actively working to strengthen our commercial offerings.

Now success in all of these areas requires the use of our full breadth of capabilities: comprehensive data, predictive analytics and our unparalleled intervention points with consumers to drive behavior change and improve health outcomes. And both Aetna and CVS Caremark have very successful employer businesses, and we're working on opportunities to create new products and services to meet the needs of these payers.

Second, we are creating differentiated products and services at the community level, driving meaningful value for both consumers and payers while improving the bottom line. Now this reflects our broad base of consumer-facing assets that is highlighted by our nearly 10,000 CVS pharmacies. And I touched on the first concept stores earlier, but importantly, our assets extend well beyond our pharmacies when you think about the role and the value that MinuteClinic, Coram, Accordant and other ancillary businesses can play. And while our community assets have the power to improve outcomes and reduce costs, they also contribute to enterprise revenue and earnings growth.

Third is the role of partnerships in accelerating innovation. And our recent announcement with Apple on the development and springtime rollout of Attain by Aetna is just one example. Applying new technologies will be a component of our consumer-centric approach to improving health.

And finally, we are establishing the optimal structure and go-to-market strategy for our health services offerings. We've been very clear about our vision of creating an open platform model that will serve the needs of all payers. And to support this goal, we are integrating existing capabilities with new products and services that will benefit all Aetna and Caremark clients and their members, and we are on track to have this in the market for the 2021 selling season.

So we're more excited than ever about our progress and the opportunities that lie ahead. We also have a good understanding of the factors that impact our business in the near term and are actively working to address them. We view 2019 as a bridge to the future, and we expect our businesses to strengthen meaningfully from the integration of CVS and Aetna's core capabilities.

Now I'm also pleased to introduce the leaders of our businesses: Jon Roberts, Chief Operating Officer; Kevin Hourican, President of CVS Pharmacy; Karen Lynch, President of Aetna; and Derica Rice, President of CVS Caremark. They'll be joining us for the Q&A after our prepared remarks. And our senior leadership team is energized by the prospects of our new company. And together with all of our colleagues across the enterprise, we are laser-focused and fully committed to delivering on the vast potential of this combination.

So let me turn the call over to Eva to walk through the key items from '18 and the details of our '19 financial outlook.

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

Thanks, Larry, and good morning, everyone. Before I get into the details of our results and guidance, please note there is a significant amount of information in the presentation we posted to our website this morning to help you understand the changes to our financials for both 2018 and 2019. Regarding 2018, while the face of the P&L is different, definitions of non-GAAP are consistent with legacy CVS. However, interest income is shifting from net interest expense to revenue to conform to insurance company presentation. With that, I'll provide some key highlights for 2018.

As Larry stated, CVS Health generated significant free cash of nearly $7 billion for the full year '18. And we used it in addition to the cash on hand to repay $5.5 billion in debt, of which $3.5 billion were scheduled maturities and $2 billion was a voluntary early repayment of a 5-year term loan. We also delivered $2 billion to shareholders through our dividend.

We delivered adjusted EPS of $7.08, at the high end of our guidance range, reflecting the addition of Aetna, with all of our businesses performing at our expectations. On a stand-alone basis, CVS Health adjusted revenue grew 2.3% in 2018, at the top end of our full year guidance range. With the addition of 34 days of Aetna's operations, which are now embedded in our new Health Care Benefits segment, adjusted revenues grew 5% to $194 billion, with HCB contributing an additional $5.1 billion after considering eliminations.

In 2018, the Retail/Long-Term Care segment delivered adjusted script growth of 8.8%, driven by our pharmacy clinical programs, comprised of increased adoption of 90-day program as well as the successful partnering with PBMs and health plans via network relationships, including additional preferred positions in a number of Med D networks.

Adjusted operating income declined by 1.2%, driven by our decision to invest a portion of the benefits we've realized from tax reform into wages and benefits. Additionally, we continued to experience underperformance in the Long-Term Care Pharmacy business. Excluding those 2 items, stand-alone Retail Pharmacy adjusted operating income grew solidly by about 5% over full year 2017. Notably, our market-leading script growth increased our Pharmacy market share to a record 26% in December.

In the PBM, adjusted claims increased 6.1% over full year 2017, driven by net new business wins and continued adoption of Maintenance Choice. PBM operating income was up nearly 1%, as expected. The formulary and cost-management strategies Caremark has developed effectively mitigated drug cost increases in 2018. Prices for non-specialty medications decreased 4.2% for commercial clients, while we also held price growth on specialty products to just 1.7%, despite even higher list price increases. We also worked to improve health outcomes and reduce member costs, successfully driving the average cost per script for plan members down for a third year in a row.

And finally, the Health Care Benefits' medical membership was 22.1 million. Government programs represented approximately half of HCB's insured membership at year-end '18, positioning the segment to drive future growth. Overall HCB operations performed as we expected. Medicare Advantage membership growth materially outpaced the market, fueled in part by our strong Star's performance. Our clinical care and service programs expanded their reach in 2018, resonating in the marketplace and strengthening the value proposition of our commercial offerings.

Adjusted gross margin for legacy CVS Health was 15.6%, up 20 basis points compared to full year 2017. This was due to mix given that the higher-margin Retail business grew faster than the PBM. Total adjusted operating expense dollars increased 12%, largely driven by the addition of Aetna's business as well as investments from a portion of the tax reform benefits into the Retail business and costs to support Pharmacy growth. As noted in our press release this morning, due to continued industry-wide and operational challenges in Q4, we recorded a $2.2 billion goodwill impairment charge on the Long-Term Care business.

Transitioning to our 2019 guidance, there are a few key changes to note. Beginning in '19, we are realigning our segments for changes to our operating model that I'll detail shortly. And our adjusted operating income guidance reflects the adoption of Aetna's legacy definition, which excludes intangible amortization. We maintain the same definition for adjusted EPS, which excludes intangible amortization and transaction and integration costs, which were consistent across both companies. A summary of the changes is included in the slides we posted to our website, along with a full GAAP to non-GAAP reconciliation. 2018 has been adjusted for comparability as appropriate.

As stated in our press release, consolidated full year adjusted EPS is expected to be in the range of $6.68 to $6.88, down from the $7.08 we reported in 2018. We expect consolidated full year 2019 adjusted operating income between $14.8 billion to $15.2 billion, with consolidated revenue in the range of $249.9 billion to $254.3 billion.

For the segments, we expect operating income in the Retail/Long-Term Care segment to be in the range of $6.6 billion to $6.7 billion and Pharmacy Services segment in the range of $4.8 billion to $4.9 billion. We expect the HCB segment operating income to be in the range of $5.1 billion to $5.2 billion.

Significant synergies will be generated by the combined business this year, stemming from elimination of duplicative corporate and operational functions, purchasing efficiencies and some medical cost savings, including formulary alignment. These synergies are expected to be between $300 million and $350 million in 2019, and we are on track to exceed our goal of $750 million in 2020.

Additionally, there will be investments in initiatives designed to set the foundation for future new product offerings. Investments are being made to further our analytics and digital capabilities, develop new programs such as chronic kidney care and enhance Aetna's clinical platform. We expect our incremental investments spending to be between $325 million and $350 million in 2019. Integration costs of approximately $550 million are excluded from our non-GAAP guidance.

We expect to deliver between $9.8 billion to $10.3 billion of cash flow from operations. We remain committed to our capital allocation priority. After the payment of our shareholder dividend, capital retention to support our insurance operation and gross capital expenditures of $2.3 billion to $2.6 billion, we will use the remaining cash available to continue to pay down debt. As we stated when we announced the Aetna acquisition, while we intend to maintain our shareholder dividend, we will not restart share repurchases or engage in large M&A transactions until we achieve our leverage target. We expect to pay down our maturities this year as they come due and have other sources of prepayable debt available to us. We expect leverage to modestly improve, and we will pay down debt in line with previous expectations.

Moving on to the segments. For the year, we expect Retail/Long-Term Care revenue to be between $85.3 billion and $86.8 billion, with adjusted operating income down about 10%. Retail is expected to continue to deliver strong adjusted script growth in the range of 4.5% and 6.8% due to continued successful execution of our pharmacy clinical care programs that drive improved adherence and patient retention.

Additionally, we will experience growth in the Medicare partnerships we formed in 2018 as well as a few new regional preferred relationships in 2019. The contraction in adjusted operating income reflects the annualization of tax reform investments and expected performance of Long-Term Care. These factors are expected to contribute nearly half of the contraction.

Continued reimbursement pressure without the full benefits of traditional offsets is also causing contraction. Historically, reimbursement pressure has been primarily offset by growth in generics as well as inflation on branded pharmaceuticals. We will experience a larger year-over-year headwind from a lower contribution from break-open generics and a diminished return on generic-dispensing increases.

The front of the store is expected to drive margins with a focus on winning in our health and beauty businesses through improved customer personalization and consumer engagement. Front store margin rate in dollars are expected to expand year-over-year.

As we look to the future, we believe CVS Retail is best positioned in the market to deal with the challenges we see. Our best-in-class clinical programs will allow us to continue to gain market share. We have strong partnerships with payers, including incentives to drive dispensing into our CVS channel. And finally, we will continue to drive efficiencies in our pharmacies through the use of technology and productivity improvement.

Now let me turn to the PBM. This segment's 2019 reported figures will be affected by 2 important reporting changes. First, our individual SilverScript PDP will move from the PBM segment to the Health Care Benefits segment, enabling us to rapidly create the best products for seniors in advance of the 2020 bid season in this important part of our business. We have restated 2018 results for comparability, and this information is also available on our website. Second, we will consolidate the pharmacy operations of Aetna into the PBM to enable us to rapidly drive efficiencies.

For the PBM segment in 2019, we expect revenue to be in the range of $136.5 billion to $139 billion, with adjusted operating income down low single digits. There are a few key elements driving 2019 PBM performance to note. As we have stated previously, price compression continues to be a factor in the marketplace. Exacerbating the impact is the cumulative effect on rebate guarantees due to lower branded inflation.

Second, the net benefits from the 2019 selling season are expected to be modest. And we expect Anthem to remain as strong a headwind, given the investments required to onboard the business on its accelerated time line. The onboarding is expected to begin in the second quarter of this year. As a reminder, the revenue for this contract will be recorded on a net basis.

Our retention rate stands at a strong 98% for 2019. In addition, Centene has notified us of their intent to move their business to their PBM partner, RxAdvance. It is expected to begin in 2019, although the exact timing is not clear at this point. The retention rate I mentioned excludes any impact from this transition. Additionally, the PBM will benefit from the segment shift. On the like-for-like basis, operating income will be down mid-single digits versus 2018.

It is clear that the PBM industry is in the middle of an environmental change given the dialogue around rebates. However, it is also clear that the PBM brings tremendous savings and value to the clients we serve. The importance of size, scale and customer relationship will continue to be paramount, and we remain focused on delivering the value our clients expect.

Finally, in the Health Care Benefits segment, we expect revenue between $67.7 billion and $68.7 billion in 2019. We expect continued strength in our government programs with top line increases driven by industry-leading Medicare growth as well as the key Medicaid wins in Kansas and Florida. We expect to end the year between 22.7 million and 23 million medical members as we expect strong commercial ASC membership gains to complement our government program growth.

A handful of other dynamics will impact HCB results, including: year 1 deal synergies will disproportionately benefit the HCB segment. Second, incremental investments will be deployed in 2019 to accelerate growth, enhance infrastructure and drive market differentiation. Third, the suspension of the health insurer fee in 2019 will impact certain operating ratios, while the after-tax impact of this suspension versus 2018 is immaterial. And finally, certain onetime benefits realized by Aetna in 2018 are not expected to repeat in 2019, and the HCB segment will be negatively affected by the segment movements discussed earlier. Excluding the segment move, the incremental investments we're making in 2019 to accelerate growth and the impact of the HIF suspension, HCB operating income is expected to grow modestly.

Turning to operating efficiencies, both CVS and Aetna have had a strong history of successful cost-productivity initiatives. And as we begin integrating the 2 companies, we are seeing the opportunity to accelerate our cost savings across the enterprise even further than originally expected. As Larry stated, we are embarking upon an aggressive cost-reduction initiative. The savings this will generate will help offset the competitive dynamics we have experienced, drive the creation of more affordable products for our customers and provide capacity that will help us achieve our financial targets as we continue to invest in our strategic and transformational initiative. We are confident that these initiatives will help drive longer-term growth in the combined business beyond 2019.

Before I wrap up, I want to touch on expectations for the first quarter and the remainder of the year. In Q1, we expect to deliver adjusted EPS of $1.49 to $1.53 and GAAP EPS of $1.04 to $1.08. As you look at the spreads for the remainder of the year, you can assume that the seasonality of our expected results this year will closely resemble that of our reported results in 2018. Year-over-year growth of consolidated adjusted operating income will be highest through the first 3 quarters as we wrap the addition of Aetna.

In the legacy CVS business, Retail, Long-Term Care and PBM, we expect to see our greatest level of year-over-year deterioration in Q1, with operating income growth in those segments improving as we move throughout the year. Adjusted operating income within HCB is expected to be greatest in Q1 and lowest in Q4.

At our Investor Day in June, we will provide you a more detailed road map to long-term growth. We will provide you with our long-term targets, including more specifics around the innovative products and services we plan to bring to market. We'll also lay out our capital structure and allocation plan to provide you with more visibility into the time line for returning more capital to shareholders while also continuing to invest in the business.

With that, I'll turn the call back to Larry.

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

All right. Thanks, Eva. Well, CVS is much better positioned to provide value to our customers and the broader community through our new enterprise model. And our diversified company is providing our stakeholders with a highly effective ability to make health care more local, more simple and less costly, while reducing our dependencies on dispensing revenue and maximizing the benefits from value-added services.

We have a number of unique offerings being piloted or launched in the coming months. And those capabilities utilize enterprise assets in a differentiated way, with the goal of increasing consumer engagement while improving health outcomes and lowering costs. As an example, expanding MinuteClinic services and incorporating CVS community assets in conjunction with Aetna analytics around a member's Next Best Action will allow us to help individuals achieve a better health outcome.

And we see tremendous opportunities ahead, whether it's improving adherence, closing gaps in care, engaging high-risk members through care managers or providing new approaches to complex disease management. Just take the mitigation of hospital readmissions. We understand the contributing factors to readmission, and we can now bring solutions to those factors. Aetna had about 470,000 hospital discharges in 2017, and about 47,000 of those were readmitted at an average cost of $14,000. If we're successful cutting that number in half, we'll remove more than $300 million of costs while creating a better patient experience.

Again, the list of opportunities goes well beyond the few examples mentioned. Importantly, many of these unique service offerings will ultimately be available to our health plan clients, creating value across the health care system. And it's this combination of assets and capabilities that will ultimately drive enterprise growth and create significant shareholder value.

So with that, let's go ahead and open it up for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Michael Cherny from Bank of America Merrill Lynch.

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

Larry, Eva, if we think about all of the headwinds in particular that you outlined going back to your conference presentation last month, I guess relative to them, what was bigger than you expected? And I guess, most importantly, as you think about all of the big ones, whether it's Omnicare, Anthem, Centene transition, et cetera, what do you view as the most transitory? In particular, where do you have the most confidence in the transitory that will be able to reverse itself or at least improve in '20 and beyond?

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

Yes, Mike, it's Larry. Thanks for the question. Mike, as you look at the transitory nature of the headwinds, you think about the impact of the investments and tax reform. That rolls off midyear of this year. You look at the inflation impact on our rebate guarantees, that peaks in 2019 and rolls off at the end of 2020. We certainly expect the Omnicare performance to stabilize and improve. And as you think about the contribution of generics, as we've talked many times, there are going to be peaks and valleys that can occur in any given year. As we sit here today and look at what that looks like for 2020, we expect that to improve. So many of these headwinds are transitory in nature. Also, keep in mind that there are parts of the business that have momentum: growth in Medicare, growth in the commercial business. We've got momentum at Retail as much as in front store growth but Pharmacy growth as well. And we're really pleased with the speed with which we're executing the integration activities.

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

And Larry, the only thing that I would add there, as Larry outlined, we also see additional opportunities to continue to manage our cost base and reduce our core to help mitigate these headwinds as we go forward.

Operator

Our next question comes from Lisa Gill from JPMorgan.

Lisa Christine Gill - *JP Morgan Chase & Co, Research Division - Senior Publishing Analyst*

Let me just, first, just go back to the guidance again. And just looking at the different segments versus our numbers and The Street, it looks like the biggest headwind year-over-year is clearly on the Retail side. Larry, when you talked about things that were transitory, not -- obviously, Omnicare being one of them. Is that the biggest driver, one, within Retail? You talked about a new type of model around reimbursement. Is that something that you believe will take hold in 2020 and reimbursement will start looking better? I just really want to understand how we think about how Retail really turns around. That would be the first part of my question. And then secondly, how do we think about that $3 billion cost-cutting initiative that you talked about a couple of years ago? Where do we see that in the numbers? And how is that coming along?

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

Lisa, this is Eva. I'll start, okay? As you think about the performance in Retail contracting about 10%, the impact of Omnicare as well as the tax reform investment, that represents about half of the contraction. And clearly, the next most significant driver is what Larry described around lower benefit from generics in 2019. In terms of the streamlining effort, that is on track, and we're delivering in line with our expectations. It's reflected in both the PBM and the Retail segments.

Kevin Hourican - *CVS Health Corporation - Executive VP & President of CVS Pharmacy*

Lisa, this is Kevin. I can also talk about the longer-term component. Our plan to improve profit outlook in Retail is focused on 3 very important things. First is to grow the top line. Increasing script volumes enables us to leverage the highly fixed cost nature of retail pharmacy fulfillment, that's the first. The second is to lower our fixed and variable costs, as Eva just spoke to, through significant productivity improvement, namely automation within the pharmacy fulfillment process as well as continued reduction in cost of goods sold through Red Oak. The third, and Larry mentioned this in his prepared remarks, is the migration to a new and improved third-party payer contracting model. We will align incentives with payers to lower overall health care costs and begin to reduce the pressure over time on the actual core pharmacy reimbursement rate.

Lisa Christine Gill - *JP Morgan Chase & Co, Research Division - Senior Publishing Analyst*

And then just as a follow-up to that, is Omnicare strategic to the company going forward? I mean, if I listen to you, Omnicare has been a headwind last year. Eva, you just talked about it being half of the headwinds for 2019. Is this a strategic asset for CVS going forward?

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

So Lisa, it's Larry. The growth opportunity with Omnicare was always focused on the independent and assisted living spaces. And those opportunities still exist, and they're consistent with our strategy of putting the customer at the nucleus of transforming care. The challenges that we have in that business are really around the skilled nursing facilities, which have been worse than we originally expected.

Operator

Our next question comes from Ralph Giacobbe from Citi.

Ralph Giacobbe - *Citigroup Inc, Research Division - Director*

Just going back, I was hoping -- and I could certainly understand the directional commentary, but are you guys willing to actually sort of quantify the drag within -- in each of the buckets? As you've sort of laid out the headwinds, it just gives more clarity on kind of the numbers and the size of each of the drags.

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

Yes, Ralph, this is Eva. In terms of -- I tried to quantify pieces of it. As you look at Retail, which has the most significant impact, the impact of Omnicare as well as the annualized impact of the tax reform investment is driving nearly half of the contraction on the Retail business. And think about the remainder, clearly, the lack of generics as the biggest driver there. Certainly, on the PBM side, the impact of the cumulative nature of the rebate guarantees affected by the lower inflation is a pretty significant driver on the PBM business. Additionally, we said it will peak in '19. We had some impact in '18. It's what moved -- it was a key element moving us to the lower end of our guidance range. And we do expect that to move through 2020.

Ralph Giacobbe - *Citigroup Inc, Research Division - Director*

Okay. All right. That's helpful. And then just maybe one quick follow-up, you've had a little more time to digest the HHS rebate proposal. Any updated thoughts there and particularly, if it gets implemented for 1/1/20? And then more broadly, you mentioned the new PBM sort of net pricing model. You expect, I think, to see a small number initially and more rapid adoption beyond 2020. I guess, how do you drive that change, particularly if employers like the legacy model? And do you see yourselves perhaps moving to just that net pricing model and just moving away from rebates altogether?

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

Yes, Ralph, it's Larry. I'll take the first part, then flip it over to Derica to talk about the new pricing model. As you look at the rebate rule, we fully support the administration's objectives to lower drug prices and out-of-pocket costs for consumers. And CVS has pioneered a number of innovative solutions that have delivered against that goal. Unfortunately, we see the rebate rule taking us backwards, not forwards. And we've been very public about the fact that 100% of rebates are turned over in the Medicare business and had been utilized to buy down premiums. You look at that dynamic, premiums will increase. And some actuarial reports have it growing as much as 52%. We actually took a step back and looked at today's Part D program. We went back to 2009. We looked at monthly premiums. 10 years ago, they were $29. 10 years later, they're $32. At the same time, you look at generics. They represent about 90% of all Part D scripts that are dispensed. So those are 2 important data points that absolutely point to premiums increasing for everyone. And the reality that yes, a small percentage of seniors may net out favorably, but again, the actuaries are estimating as many as 70% of beneficiaries are going to be worse off. So one of the concerns that we have is that fewer beneficiaries sign up for Part D. And then you look at the estimated cost of $200 billion over 10 years, and it puts taxpayers on the hook and branded pharma ends up with a profit windfall. There are certainly readily available solutions in the commercial space that can be applied to Medicare, and you look at what those potentially could be. We work with commercial clients today to reduce out-of-pocket costs with point-of-sale rebates and the utilization of a preventive drug list. We think programs like that are far better solutions than the proposed rule. And we also have -- we've talked about the realtime benefits tool in Caremark. Kevin's got a similar program in our Retail pharmacies. And both of those tools have reduced out-of-pocket costs for consumers. So we're certainly weighing in during the comment period with our concerns with the rebate rule, but more importantly, what we believe the appropriate solutions are to address the root cause of what we're trying to solve for. Derica?

Derica W. Rice - *CVS Health Corporation - Executive VP & President of CVS Caremark*

Ralph, this is Derica. In regards to our new pricing model, what we're calling the Guaranteed Net Cost model, we've had 2 clients who adopted for 2019. In addition to that, we've already provided to all of the benefit consultants draft contract language. So they've been able to walk through and see all of the elements in terms of the fine print in the details. The feedback, thus far, has been very positive. So we will look to continue to drive a more rapid adoption through the remainder of '19 and, more specifically, for the 2020 period. In terms of rebates, whether we have rebates or discounts, what we really want is still the opportunity, and this is kind of piggybacking on the HHS roll question, our ability to execute formulary management, which is the methodology we've been able -- and the tool we've been able to use historically to be able to create rebate or discounts from manufacturers to create value for our clients and their members. So as long as we have access to that wherewithal to be able to do that with the manufacturers, we will be able to execute the GNC model. And really, what this means is getting to the lowest net cost. It is not a focus on aggregate rebate value.

Operator

Our next question comes from Justin Lake from Wolfe Research.

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

First one of two, discuss rebate guarantees and the break-open generics, I'm just trying to understand '19 to 2020. So it sounded like, Larry, you said break-open generics get better in 2020 versus 2019. Can you give us an order of magnitude there? And then same thing on rebate guarantees. It sounds like it peaks in '19, but it gets better in 2020 in your mind? And maybe you could tell us about some of the remediation that you've assumed in these -- in your guidance around rebate guarantees.

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

Yes, Justin, this is Jon. I'll take the generic question first. So the overall dollar amount of generic launches in '19 is similar to what we saw in '18, but there are some key differences. So you heard us talk about less value from break-open generics in '19 compared to '18. And that's primarily due to the timing of the launches, leading to slower progress in '19 to the break-open status. But there are also more generics launching in '19 compared to '18 that are single-sourced generics, where we're unable to optimize our profitability during that exclusivity period. And as a result, these generics for the most part are headwinds in '19. And finally, in '19, we're seeing generics that launch with limited competition, stay with limited competition even after the exclusivity period expires. And this is driven by many factors, including manufacturing complexity and regulatory approval time lines. But as we look forward into 2020, based on what we know today, we see 2020 improving from where we were in '19.

Derica W. Rice - *CVS Health Corporation - Executive VP & President of CVS Caremark*

And Justin, this is Derica. In regards to the rebate guarantees and exposure, just recall from both Eva and Larry's remarks that we anticipate that the rebate exposure peaks in 2019, and we anticipate that it will dissipate over the '20 and 2021 period. And we've also been able to go back and adjust our underwriting models to now we're assuming a mid-single-digit inflation rate. So much (inaudible) working with current trends.

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

Okay. And if I could just sneak a follow-up, the last number you gave us on rebates' retention was $300 million, I believe. And that's net of payouts for rebate guarantees. Given that rebate guarantees have gone up, can you give us an updated number there?

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

Justin, this is Eva. That was a stand-alone legacy CVS PBM. And I would say, it's in the same ZIP code, if you will, in terms of that overall 2 to 3 percentage points.

Operator

Our next question comes from Ana Gupte from SVB Leerink.

Anagha A. Gupte - *SVB Leerink LLC, Research Division - MD of Healthcare Services & Senior Research Analyst*

My question was about on the health benefits side. The medical loss ratio, you had said that the experience-rated book would create a reset. It's a bit more than we had anticipated. I wanted to know if this is kind of a onetime thing. And can you talk about on the commercial side, what the implications were there for membership on either retention and/or new growth? And also, if you -- when you're planning to go to market with Aetna and the Caremark book together? Is it going to be midyear this year, in 1/1/20, maybe later?

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

Ana, this is Eva. I'll start. As you look at our guidance for the MBR, it's about 84%. There are a couple of things that I would call out. First, obviously the mechanics of the HIF as well as if you look at the mix of our business, we have very material growth in the government services business, which obviously also increases that MBR. And it's early in the year, and we feel it's important to be prudent as we look at these estimates.

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

Yes, Ana, just to answer your question on when we'll go to market with the Caremark book, obviously, we're in the process of evaluating where we have opportunities. We are rapidly looking at where we have medical and not pharmacy and vice versa, working very closely with Derica. We are building products and service capabilities, so that we can go to market. And you should expect us to see -- go to market later this year, early in '20.

Anagha A. Gupte - *SVB Leerink LLC, Research Division - MD of Healthcare Services & Senior Research Analyst*

If I could just sneak in a follow-up on that, so also on the tax reform, Aetna had seen some pressure on MLR rebates. Will this combination help you on that? Might that start in 2020? And I think you also had talked about enterprise value in your last communication post-close. And is that going to impact how you price your Aetna book? Because you do have value that's created now from the PBM and Retail that wasn't there earlier?

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

Yes, relative to pricing, we will factor all that and consider that in our pricing. But Ana, what I would tell you is we'll continue to maintain pricing discipline on our commercial book. But we'll take the value of a combined organization or the value that we expect to capture from additional services in consideration when we do price our book.

Operator

Our next question comes from Steven Valiquette from Barclays.

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

So for the HCB segment, the slides include a comment that excluding segment shift impacts, incremental investments and the impact of the HIF, the operating income is expected to grow modestly over 2018. I think some investors might have been expecting that profit growth to be a little bit stronger in '19, just given the robust Medicare Advantage membership growth for Aetna, actually both last year and this year. I know it's a general notion that new MA lives aren't that profitable in year 1. But maybe you could just give a little more color, high level around the Medicare Advantage membership growth in 2019, maybe just frame it in terms of top line growth versus profit growth within HCB.

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

Yes, Steve, this is Eva. I think a key aspect is we noted in our prepared remarks that we're making significant investments in terms of transformation. There are some of that affecting the HCB segment, so the modest growth is obviously taking into account that impact.

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

So let me just comment on just general Medicare growth in '19 and '20. Both years, we are above-industry growth. You have to consider when you look at our Medicare business, the split -- the mix between individual and group, obviously, there are different margin profiles on those books. If you think about 2020, we are exceptionally pleased with the growth that we have for 1/1. As you can -- as you've seen, we're above-industry growth. That is really, truly reflecting the number of years that we've been investing in Medicare. It's reflecting our Star's performance. It's reflecting our expansion into different geographic counties and really tight management of our benefit product. What I would also say to you is that the way to think about our growth for 1/1, think about it half group and half individual.

Operator

Our next question comes from Ricky Goldwasser from Morgan Stanley.

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

Larry, going back to the HHS rebate rule, I understand the questions that you raised. But if -- assuming that the rule is finalized effective 1/1/20, it seems that there's going to be a change to the business model as we know it today. So one, can you fully offset with premium increase an impact on the PDP business? Two, what would be the implications for your commercial business? I.e., based on past experience, how long does it take before we see the spillover effect to commercial changes? And three, you're in the hole on the commercial book on rebate guarantees. Is the new rule a material enough change that will allow you to go back to your commercial customers and trigger a change in current contractual terms that can help offset that?

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

Yes, Ricky, it's Larry. In terms of your first question around the offsets, yes, we would underwrite that with a different set of assumptions, Ricky. And some of that goes back to my earlier comments. The concern would be will people deselect from a Part D program because of the increase in monthly premiums. We know that from all the research we've done over the years that beneficiaries, that's the first thing they look at. And SilverScript has been successful growing with holding down that monthly premium level for the reasons that I touched on earlier. Your second point, Ricky, around commercial. Listen, our sense is what is it that our clients want and value? And I would sit here today and say, "Broadly, our commercial clients value the same elements, that the Medicare Part D program works, that they want to use the rebates and discounts to buy down the monthly premium." So I'm not sure that I see a rapid adoption in the commercial space for that reason. And Ricky, the other thing that I would point out is, I think, many people are aware that Caremark introduced a new plan this year. It was called Allure, where it priced -- it took the rebates and applied point of sale. We had a very, I would say, small number of seniors enroll in that program. It was around 20,000. And we think one of the barriers to that was the increase that we saw in the monthly premium.

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

Okay. So a follow-up question here. One, just if you can refer to -- if the change happens, can you go back and change some contractual terms? And then a second follow-up is, obviously, 2019 is a transition year, and you're going to give long-term guidance on your Analyst Day. But it's been over a year since you gave us year 2 accretion goal. So can you give us any update there? What type of growth should we expect next year?

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

Yes, Ricky. In terms of the other question on can we go back to clients should there be a material change in how the programs are written, the answer to that question is yes, okay? And in terms, Ricky, for a 2020 outlook, we're not going to provide that today. It's -- we're working diligently, recognizing that we have made great progress on the integration work that was tied to the synergy goals that we've talked about. And as you think about the regulatory pathway, quite frankly, it was very late in that process that we were able to begin the transformation work in earnest. So we're pretty pleased that we've got concept stores up and running. We've got a number of pilots in the market and a whole another series ready to go to market to learn and understand. And that is our primary objective, to complete more of that work. So when we get to June, we will be able to provide more of a long-term outlook.

Operator

Our next question comes from Ann Hynes from Mizuho Securities.

Ann Kathleen Hynes - *Mizuho Securities USA LLC, Research Division - MD of Americas Research*

I actually just want to follow up on Ricky's question because I do think 2020 is important. Because when you closed the deal, you did give some directional guidance that's mid-single digits. And if you adjust for tax reform, it would suggest a mid-$8 range. And the reason I bring it up is because that's where consensus estimate is now. So I know you don't want to comment on it. But what do you think that we should consider in our models as the biggest change to your business model since you gave that guidance in December of 2017, I believe? So that's one. And secondly, on the Retail operating profit decline, if you ex the Omnicare and I think you said the tax reform investment is down 5%. And I know you say it's because break-open generics is less of an offset, but I still feel like that's very low. Can you give us more detail on what's happening there, so we put it on our models going forward? Because it just seems a bigger decline than I would think.

Kevin Hourican - *CVS Health Corporation - Executive VP & President of CVS Pharmacy*

Yes, Ann, this is Kevin. I'll take the Retail question, and then Eva will talk about 2020. The primary headwind in the Retail profitability excluding Long-Term Care and the tax investment is in pharmacy reimbursement. It's impacting small operators and big operators. It's a secular headwind impacting everyone. What we talked about is a tailwind that, typically, is utilized to help us blunt that reduction is the generic wave. And Jon covered it well that, that value year-over-year is down. Eva also mentioned in her prepared remarks that there has been effect from branded inflation that helps that blunting as well, and that number is down year-over-year. So we're seeing a consistent headwind. It's the 2 tailwinds themselves that reduced in value year-over-year. And as I mentioned a few moments ago, our plan to address that for 2020 and beyond is to accelerate our top line growth. The good news in our Retail business is we are winning in the top line. We're taking market share in both the front and Pharmacy business. We're resonating with consumers, growing share of wallet with consumers and taking market share. What we need to do more for 2020 and beyond is increase the year-over-year value of productivity improvement. We have some compelling innovations coming in technology improvement that can help automate things that are currently done manually within the pharmacies. And I'll just repeat, the most important thing we need to do is to make a pivot in our third-party payor contracting. We are going to lead to change there to migrate to a new method of doing pharmacy contracting. We're going to start with ourselves. So by owning a large insurer and owning the largest PBM, we can lead that change by structuring a contracting relationship, that if we can lower overall health care costs, we can take some of the burden off of the annual reimbursement reform. And where that will come from is the last thing I'll say is we can prove through technology and clinical care programs that we can improve medication adherence. We can maximize the formulary compliance that Derica spoke to in his remarks. We can do things that are net new like reduced hospitalization through our clinical outreach program, saving Aetna money, and then we can share in the benefit of that from the Retail segment. We intend to bring that model to the other payers, and 2 of the other payers also own an insurance company.

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

And I just want to emphasize the last point that Kevin just mentioned, because I've come to appreciate when you look at the Aetna business today, more than 50% of their claims have some type of outcomes-based reimbursement tied to that. And it's all on the medical side with providers, okay? Yet, we have -- Pharmacy has not penetrated that. And this new model is going to demonstrate the role that Pharmacy can play in terms of affecting and improving outcomes. And I think it's one of the big unlocks as you think about an open platform concept that we could make elements of broadly available in the market.

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

So Ann, this is Eva, I'll go back to your 2020 question. And as Larry said, it's still really early to give 2020 guidance or expectation, but let me try to provide you some color. In terms of the accretion numbers that were provided back when the deal was announced, it's really difficult at this point in time to speak to those. Given the timing of the deal close, you'd have to mix and match periods as well as the changes related to tax reform. But what is 100% clear is that Aetna is performing at or better than our expectations. We absolutely stand behind the estimates of the value being created by the deal. And as we've said, we're tracking ahead of our synergy number, year 2 synergy number of 2020. The factors affecting, what I'll say, the legacy CVS businesses, as you think about 2020, all of those factors will either improve or phase out. The tax reform investment obviously is complete. The impact of the rebate guarantee peaks in '19 and is reduced in 2020. And we expect both Omnicare and generics to improve in 2020.

Operator

Our next question comes from Robert Jones from Goldman Sachs.

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

I guess just to follow up there on the synergies. It clearly sounds like you're still on track. I mean, maybe one of the other sides of it that was a little bit larger than I think we would have expected was the incremental spending in order to achieve those synergies. So just on the numbers that you provided for this year, could you talk a little bit about what that spend is exactly? And I know you said, Eva, that HCB would disproportionately benefit from the synergies this year. Is that safe to assume where the incremental spend would also come?

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

Yes, Bob, thanks for the question. So as we think about the additional investment spending, it's in the $325 million to $350 million range. I would put that spending into 2 large buckets, right? Supporting transformation and includes investments in our clinical platform to more effectively engage members, our chronic care initiative and other initiatives aimed at improving outcomes and lowering cost. The other area that we're continuing to invest in and expand our investment is digital and improving the digital and mobile experience for members and customers across all of our businesses. And we're making investments in our health cloud software platform. So a large amount of these investments do affect the Aetna business as there was 0 in 2019, if you will, in the denominator for which we're comparing.

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

Okay. And then safe to assume that as we roll beyond '19, these costs should reduce would just be the quick follow-up. And then the other question I had, more housekeeping, was just as we look at the guide for HCB housekeeping, is prior period development included or excluded from that guidance?

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

So Bob, I'll take your last question first. There is no -- consistent with Aetna's legacy practices, there is no prior period development included in our guidance. In terms of investments in the business, yes, I do think as the investments will step down over time, but we will continue to invest in our business as we're evolving to our new model with the consumer at the center.

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

And Bob also, just keep in mind to that point that as you've heard us talk on the Retail side, more on the CapEx side, we have the opportunity to repurpose capital that we would have spent in the areas that can be dedicated to our activity here. So that's one of the reasons why you don't hear us talking about it in that regard.

Operator

Our next question comes from Charles Rhyee from Cowen.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

I just want to go back to Omnicare real quickly here. You've kind of written off maybe upwards of half of the value of what you've kind of put into it initially when you consider the debt you took on as well. It sounds like there's 2 pieces you're talking about, right? The piece that you're interested in, which was the independent and assisted living market versus the SNF market. When you talk about the turnaround here, is it that you expect initiatives to grow the business in assisted living, that's going to take off? Or is it that you think the declines in the SNF business are going to slow? And you've been talking about this for a little bit. What's kind of giving you the confidence -- what gives you the confidence here that you would expect that to turn as you get into '20?

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

Yes, Charles, it's Larry. And just one quick comment on that, and then I want to flip it over to Jon. As you look at the Omnicare business, don't lose sight of there was a specialty component of that business, which has been fully integrated and quite successful for the business. So I don't want to lose that element of the acquisition.

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

Yes. And Charles, this is Jon. So what gives us the confidence that we can stabilize the Long-Term Care, that's the SNF. We have to think about stabilizing that. We've invested in account management personnel, so that they're providing higher levels of service to the facilities. We've seen significant improvements in our service levels, and our retention rates are improving pretty significantly. And we're putting technology in that assist these facilities in communicating with the pharmacies. So we think service ties directly to retention, and we've made significant improvements there. And then we still are very bullish on our ability to grow in assisted living. So we've implemented a new service model, we call them community care centers. So that there's a single point of contact with that community staff for senior living. That was not the case prior to this past year. And then we've introduced some tools that we think are going to be very attractive to these facilities, like multidose packaging that is better than what's available generally in the market with barcode scanning. And then we're also leveraging our CVS retail pharmacies for stat deliveries to these facilities. So these pharmacies are closer than the Omnicare pharmacies. They can respond more rapidly and actually develop a relationship, a local relationship with those facilities, along with the Omnicare pharmacy. So we think we'll be able to not only grow our penetration rate in these assisted living facilities, but we're seeing existing clients, where we didn't have all of the assisted living facilities, actually give us more of their facilities because of these services and changes and enhancements that we've made.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

My understanding -- just to follow up on that, my understanding is in assisted living, the part of the problem with that market was that the facilities themselves didn't think of themselves really as health care providers, really more as residential communities. Is that behavior starting to change? Because it seems like a lot of the issues that you're discussing here are actually issues probably that Omnicare dealt with years ago as well. And so it kind of points to more of a structural issue, particularly in the SNF market, I guess. Any kind of structural changes you're either seeing that you think can be a positive as you kind of move forward here?

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

I think the structural change we're seeing in senior living or independent living, they're trying to be able to provide continuity of care as people progress through the different phases of aging and they move from independent living to assisted living. And so we think our value proposition will resonate even more based on these changing dynamics and what we've seen historically.

Operator

Our final question comes from Kevin Caliendo from UBS.

Kevin Caliendo - *UBS Investment Bank, Research Division - Equity Research Analyst of Healthcare IT and Distribution*

One question I had just on the Aetna business, the health benefits business. If you could just tell us on an apples-to-apples basis without any of the shifts between the segments and the like, what Aetna would have looked like, excluding any cost shifts that you may have done into that segment or the like. What are we -- what would we be looking at? That's the first question. And the second question, can you talk about the magnitude of the Centene loss? Should we expect to see that revenue loss? And how would it roll and impact the PBM margins positively or negatively and -- going forward?

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

So Kevin, this is Eva. I'll take the first question regarding Aetna's performance without the shift. What we're seeing, the most clarity I can give you here is without the shift and some of the things we've called out, we expect to see modest growth. The business has tailwinds behind it with the growth on membership in both commercial and government space, benefiting nicely from the synergies, but we're also making investments. So the best on a same-same basis, some modest growth on the bottom line. Obviously, normalizing for the health insurance fee impact.

Kevin Caliendo - *UBS Investment Bank, Research Division - Equity Research Analyst of Healthcare IT and Distribution*

Right. Okay. And then on Centene?

Derica W. Rice - *CVS Health Corporation - Executive VP & President of CVS Caremark*

Kevin, this is Derica. In regards to Centene, just keep in mind that it will be a multiyear migration. We anticipate it will start in 2019, likely to peak in 2020, and there's probably a residual in 2021. And as Centene is migrating, they're looking to move to their own PBM platform, RxAdvance.

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

And Kevin, just to add one thing to Derica's point, while the exact timing with these large changes, you don't know exactly how the rollout will go, in our guidance range, we had made estimates within the range around our expected migration.

Kevin Caliendo - *UBS Investment Bank, Research Division - Equity Research Analyst of Healthcare IT and Distribution*

Got it. And just, I guess, one more on the WellCare, the PDP business that you sold to WellCare, how is that incorporated into the numbers now? Is it? And what was the magnitude?

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

So WellCare, it's a transition year. The economics still continue to benefit Aetna.

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

Yes, they benefit Aetna. They're still in the Aetna results as we're transitioning it out.

Kevin Caliendo - *UBS Investment Bank, Research Division - Equity Research Analyst of Healthcare IT and Distribution*

Okay. Great. I just wanted to make sure that they were still included in there.

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

All right. So listen, we know this was a long call. We know there's a lot of information, a lot of questions. And as is always the case, Mike will be -- Mike and his team will be available for any follow-ups. And I'm sure we'll see many of you soon. Thanks.

Operator

This concludes today's conference. You may now disconnect.