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CVS Health Corporation (CVS) CEO Larry Merlo on Q3 2019 Results - Earnings Call Transcript

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Q3: 11-06-19 Earnings Summary

Press Release *Slides*

EPS of $1.84 beats by $0.07 | Revenue of $64.81B (37.11% Y/Y) beats by $1.86B

Earning Call Audio

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CVS Health Corporation (NYSE:CVS) Q3 2019 Results Earnings Conference Call November 6, 2019 8:00 AM ET

Company Participants

Valerie Haertel - Senior Vice President, Investor Relations

Larry Merlo - President, Chief Executive Officer

Eva Boratto - Chief Financial Officer and Executive Vice President

Kevin Hourican - Executive Vice President CVS Health & President of CVS Pharmacy

Karen Lynch - Executive Vice President CVS Health & President of Aetna Business Unit

Derica Rice - Executive Vice President CVS Health & President of Caremark

Jonathan Roberts - Executive Vice President & Chief Operating Officer

Conference Call Participants

Lisa Gill - JPMorgan

Lance Wilkes - Sanford Bernstein

Charles Rhyee - Cowen

Ricky Goldwasser - Morgan Stanley

Michael Cherny - Bank of America

George Hill - Deutsche Bank

Ann Hynes - Mizuho Securities

Robert Jones - Goldman Sachs

Ralph Giacobbe - Citi

A.J. Rice - Credit Suisse

Steven Valiquette - Barclays

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the CVS Health Q3 2019 Earnings Call. At this time, all participants are in a listen-only mode. After the speakers presentation, there will be a question-and-answer session. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Valerie Haertel, Senior Vice President of Investor Relations. Thank you. Please go ahead.

Valerie Haertel

Thank you. And good morning everyone. Welcome to the CVS Health third quarter 2019 earnings call. As a reminder, this call is being recorded. I am Valerie Haertel, Senior Vice President of Investor Relations for CVS Health. I am joined this morning by Larry Merlo, President and CEO; Eva Boratto, Executive Vice President and CFO.

Following our prepared remarks, we'll host a question-and-answer session when Jon Roberts, Chief Operating Officer; Karen Lynch, President of Aetna; Derica Rice, President of Caremark; and Kevin Hourican, President of CVS Pharmacy will also join us.

In order to provide more people with the chance to ask their questions during the Q&A, please limit yourself to no more than one question with a quick follow-up.

In addition to this call and our press release consistent with our practice, we have posted a slide presentation on our website. Our Form 10-Q was filed this morning and is available.

Please note 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 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 concerning forward-looking statements 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 discussion of these non-GAAP measures and the comparable GAAP measures in the earnings press 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 one year following the call.

Now, I'll turn the call over to Larry.

Larry Merlo

Well. Thanks, Valerie. Good morning everyone and thanks for joining us. In the third quarter, we continued building on our positive business momentum delivering adjusted earnings per share of $1.84, exceeding the high end of our guidance range.

Importantly, this performance was driven by strong operational execution across our enterprise with all three segments performing in line with or above our expectations. And I'll note that $0.04 of our Q3 performance was the result of net realized capital gains and favorable prior year's development.

We generated strong cash flow from operations which enabled us to continue to make progress on deleveraging, all while investing in our core businesses and returning capital to our shareholders through dividends.

Given our year-to-date success in executing against our strategic plan, we are raising and narrowing our adjusted earnings per share guidance range to $6.97 to $7.05. And Eva will provide a more in-depth review of our results and increased guidance in her remarks.

Now, as we continue to transform CBS into the country's leading consumer health company, we are successfully executing on our long-term growth strategy across the four-key enterprise-wide priorities we shared at our June Investor Day.

Importantly, our teams are working together across the enterprise to maximize value to our members, consumers, patients, and shareholders, and our operational and financial performance this year reflects their efforts.

We continue to use our unmatched combination of assets by enhancing and creating products and services to further grow and differentiate our businesses, our first strategic priority.

In our Retail, Long-Term Care segment, we continued to drive strong prescription growth using our data and analytics capabilities through targeted proactive member communication.

A key differentiator of our retail stores is our ability to meet members and consumers where they are to deliver local personalized care through our MinuteClinics and now our HealthHUBs making healthcare more accessible and affordable. And our approach is clearly resonating in the marketplace and is exemplified both by our continued share gains at retail and the early success of the HealthHUBs.

Now in terms of early impact, our HealthHUBs in Houston, which now have about eight months of performance have continued to outperform their control group with higher script volume and Minuteclinic visits along with higher front store sales, traffic, and store margin.

This favorable performance and the incremental value we expect will be derived from the expanded utilization of the hubs gives us further confidence in our planned rapid rollout, and we are on track with three additional metro areas with approximately 50 hubs operational by year-end along with our plan to have 1,500 hubs by the end of 2021.

The value we expect our HealthHUBs to deliver stems from various sources. First, increased earnings contributions from the greater use of our new and enhanced products and services.

Second, improved medical cost savings in Aetna's book of business, as we deploy our capabilities to address the unique needs of the member populations we serve driving value to our Health Care Benefits segment.

Our plan design innovations aim to incentivize members to utilize more cost-effective settings and providing our pharmacies with integrated medical and pharmacy data allows for improving the delivery of a member’s next best health action to impact behavior changes and improved health outcomes.

Third is our unmatched capability through our open-source approach in extending consumer-centric offerings to our health plan relationships across the CVS health enterprise. And our new product and service offerings have a direct impact on the overall healthcare costs of the clients and partners serviced by CVS Caremark and CVS Pharmacy, and they are making a difference in our market positioning with these clients and partners. And all of this leads to a fourth driver of value, and that's the resultant benefit of increased customer satisfaction and retention.

Now, our opportunity to differentiate our offerings at the community level received another boost with a recent designation earned by our MinuteClinics. CVS Health professionals who staff our clinics, which again are foundational to our HealthHUB expansion, have earned a pathway to excellence designation from the American Nurses Credentialing Center for the quality services they provide. And MinuteClinic is the first and only retail clinic to receive this elite designation.

So as more hubs come online toward our goal of 1,500, we will continue to update you on our performance and the benefits of our integrated health care approach for consumers.

For our Pharmacy Services segment, we continue to deliver solid performance driven by growth in specialty, strong volume in our Maintenance Choice program, and continued improvement in purchasing economics.

As for the 2020 selling season, it's nearly complete with gross new business increasing $1.1 billion and net new business improving by approximately $1 billion since our second quarter update in August.

The 2021 selling season is now underway, and we are well positioned with our product offerings and our sales teams are engaging in productive conversations, identifying innovative ways to serve both new and existing clients.

To that end in the quarter, we successfully renewed our relationship with the Federal Employees Health Benefits program through December 2021. And this renewal includes both our mail and retail contracts and represents an opportunity to continue to strengthen our client relationship.

Our Health Care Benefits segment is also well positioned for growth heading into 2020 and we are building momentum with our new enterprise offerings, which will differentiate us in the marketplace. Our customer value proposition has been further reinforced by the most recent Medicare Advantage Star ratings data released by CMS last month.

And Aetna's Medicare Advantage plans earned an overall weighted average of 4.3 out of five stars for 2020, with 76% of our Medicare Advantage members enrolled in plans rated at least 4.5 stars, and that's based on our September 2019 membership and that's also the highest percentage among publicly traded companies with over 250,000 Medicare Advantage enrollees.

Our 2020 star ratings drive more favorable bonus payments and bid rebates, enabling enhanced product offerings in 2021. And this year's star ratings demonstrate the success of Aetna's approach to growing our Medicare business across the country, while maintaining best-in-class quality.

Turning to Medicaid. We were recently awarded Medicaid lives in the Texas Star Plus program and the West Virginia Children and Youth Program. And these wins reinforce our commitment to Medicaid and speak to the strength of our Medicaid services and capabilities allowing us to build upon existing relationships with two very important state partners.

Now we’re also encouraged by the strong client interest in our new integrated capabilities, including our HealthHUBs and these capabilities will be a core component of our value proposition for the 2021 selling season.

We’re also excited about our recently launched Healing Better program, a transitions-of-care program intended to improve the recovery process from joint replacement procedures.

Healing Better is another example of the power of our combination to provide enterprise solutions to improve patient experiences. And we're excited to incorporate this offering into Medicare Advantage plans in select geographies in 2020.

Moving to our second strategic priority, delivering transformational products and services, we are continuing to advance innovative pilot programs, and introduce new and innovative offerings. In the third quarter, our oncology pilot continued to rollout across selected geographies.

We also rolled out the first phase of our chronic kidney care management program to Aetna and Caremark clients for early disease detection and care management development. And with several hundred members under management, we are moving on to the second phase of the program, which is the face-to-face counseling around different dialysis modalities.

And I should also mention that our home hemodialysis clinical trial is progressing as expected with our first two sites active. And we are confident that, we will complete the trial on our previously discussed time line. With our third strategic priority, we are developing and enhancing programs that encompass our consumer-centric technology infrastructure.

And as previously announced, our CarePass subscription service went live nationally in the third quarter. And we have already enrolled more than one million members in less than two months, which has exceeded our expectations for this recently launched membership program.

In our Health Care Benefits segment, we have expanded the use of our proprietary NovoLogix technology for prior authorization and claims management in our commercial population. And given the proven success of our NovoLogix capabilities we are confident in our ability to drive cost savings and efficiencies for our clients, who participate in those programs.

Additionally, we now have more than 82 million consumers and members engaging with our enterprise through text messaging, and that's an increase of 7% from last quarter. And we're encouraged by the increased engagement we have experienced across our digital programs.

Moving to our fourth strategic priority, modernizing our enterprise functions and capabilities, again, we're making progress and are on track to see the initial benefits beginning in 2020. And we have aligned teams around simplifying our service operations embedding intelligent automation to streamline routine processes and further advance our digital footprint.

These initiatives are expected to further enhance our self-service capabilities by eliminating unnecessary member and patient mailings, as well as reduce incoming call volume across our businesses.

And we continue to expect to generate $1.5 billion to $2 billion in run rate net savings in 2022 for enterprise modernization. And I should also note this is in addition to the $900 million run rate of projected integration synergies in 2021 that we have previously discussed.

Another exciting accomplishment related to our investments on the CSR front is CVS Health being named to the prestigious Dow Jones Sustainability Index for the seventh consecutive year and for the first time added to their world index. And we are proud of this recognition which is a true indication of our industry leadership in the area of corporate sustainability and our commitment to improving the health care system.

And with that, I'll turn the call over to Eva to walk through our financial results and guidance.

Eva Boratto

Thanks, Larry. And good morning, everyone. As Larry said, strong performance across the enterprise drove our third quarter results. Adjusted earnings per share of $1.84 was above the high end of our guidance, including $0.04 attributable to non-recurring items, generated by net realized capital gains in prior years development. Health Care Benefits exceeded our expectations while Pharmacy Services and Retail/Long-Term Care were in line. The quarter also benefited from lower interest expense.

Consolidated adjusted revenues grew 37.1% in Q3 of 2019, also exceeding our expectations. This year-over-year increase was largely driven by the addition of Aetna as well as higher volume in both the PBM and Retail/Long-Term Care segment. The Health Care Benefits segment, which includes our SilverScript PDP business contributed $17.2 billion of revenues for the quarter.

Adjusted consolidated operating income grew 48.9% compared to last year, primarily due to the addition of the Aetna business. Health Care Benefits contributed $1.4 billion and we experienced growth in the PBM, which was partially offset by a decline in Retail/Long-Term Care.

Looking at our results by segment and starting with Pharmacy Services. Total revenues increased 6.4% with adjusted claims volume up 9.3% year-over-year. Drivers included net new business, particularly in specialty related to the IngenioRx onboarding and the continued adoption of our Maintenance Choice offerings.

PBM adjusted operating income increased 5.7% versus Q3 of 2018, due to increased claims volume the shift of Aetna Mail order and specialty operations into our Pharmacy Services segment and improved purchasing economics.

We continue to mitigate our rebate guarantee exposure through formulary compliance and have experienced a larger-than-expected benefit from generic launches primarily in specialty. These improvements are partially offset by continued price compression. Brand drug inflation remains consistent with our previous expectations.

Moving to Retail, Long-Term Care, the segment performed in line with our expectations with total revenues up 2.9%, driven by higher prescription volume. We delivered strong adjusted script growth of 6.4% with comp scripts up 7.8%, primarily driven by the continued adoption of our patient care programs. Our share of retail scripts increased approximately 110 basis points to 26.6% in Q3 versus the same period last year.

Additionally, front store comp sales increased 60 basis points, driven primarily by continued growth in health and beauty sales including cough and cold. Retail/Long-Term Care third quarter adjusted operating income declined 6.5% year-over-year, primarily driven by continued reimbursement pressure, partially offsetting the decline with continued script growth and front-store margin improvement as well as the benefit of generics, where we have seen some improvement.

As part of our ongoing review of our asset portfolio and focus on driving greater returns, in the quarter we made the decision to close approximately 75 retail pharmacy stores during 2020, the majority of which are nearing the end of their lease term. This resulted in a $96 million GAAP charge in the Retail/Long-Term Care segment. We believe these decisions will generate enhanced longer-term performance.

Our real estate footprint remains very productive and we will continue to look for opportunities to further improve the performance in our portfolio. Lastly, our Health Care Benefits segment delivered better-than-expected results for the quarter due to prior year's development and net realized capital gains.

Total revenues of $17.2 billion continued to benefit from strong growth in government business. Total health MBR of 83.3% benefited from favorable prior period development across all our core products. Last quarter, we highlighted modest pressure in a specific portion of the lower end of our middle market commercial book. During this quarter, we saw modest improvement in this business and we continue to expect our MBR for the full year to be above the midpoint of our guidance range of 84% plus or minus 50 basis points.

Our days claims payable was 51 days for Q3, compared to Q2, days claims payable increased by three days due to the seasonality that is typical of our PDP business. We remain confident in the adequacy of our reserves and our ongoing reserving process.

Within our Corporate segment, we realized $32 million of net realized capital gains in the quarter. Corporate segment expenses increased sequentially and year-over-year primarily due to investments in our transformation and modernization programs.

Moving to capital management. During the third quarter, we continued to make progress on our deleveraging efforts which resulted in a net debt reduction of approximately $2.9 billion.

In addition to paying off over $1.5 billion term loan $850 million of scheduled maturities, we completed a $4 billion tender offer for our outstanding senior debt and issued $3.5 billion of senior debt at favorable rates during the quarter.

We have now repaid approximately $8 billion of net debt since the close of the Aetna transaction. And we remain focused on deleveraging and achieving our leverage target of below three times in 2022.

Turning to cash flows and dividends. This quarter, we generated strong cash from operations of $2.9 billion from improved working capital and earnings performance. We also returned more than $600 million to shareholders through dividends. With that let me turn to our revised guidance for 2019.

As Larry mentioned in light of our third quarter performance, we are narrowing and raising our consolidated full year adjusted earnings per share guidance range to $6.97 to $7.05 million compared to prior guidance of $6.89 to $7.

Our full year guidance reflects an aggregate of approximately $0.20 of prior year's development and net realized capital gains that we have recorded in the first nine months of this year.

We are also raising our consolidated full year total revenues expectations to $251.6 billion to $254.2 billion and raising and narrowing our adjusted operating income expectations to $15.22 billion to $15.40 billion. Additionally, we're on track to deliver at least $400 million of integration synergies this year.

Now a few highlights on our segment. There is additional detail in the slide presentation we posted on our website. We are increasing our expectations for the Pharmacy Services segment with adjusted operating income now in the range of $5.1 billion to $5.16 billion reflecting the momentum in the business. We're maintaining our full year adjusted operating income range for the Health Care Benefits segment of $5.18 billion to $5.24 billion reflecting year-to-date performance including favorable prior year's development and net realized capital gains as well as our latest projection of investments required to onboard 2020 new business.

We are narrowing our full year adjusted operating income range for our Retail/Long-Term Care segment to $6.68 billion to $6.74 billion. And we are lowering our interest expense estimates to our strong cash flow and impact from the net pay down of debt.

Our updated full year 2019 GAAP EPS guidance range is $4.90 to $4.98, reflecting our year-to-date performance the negative impact of store closures and the loss on the early extinguishment of debt.

We're maintaining our full year 2019 cash flow guidance expecting to deliver strong cash from operations between $10.1 billion and $10.6 billion and have increased our projected cash available to pay down debt to $4.7 billion to $5.1 billion of which $4.7 billion has been used to pay down debt year-to-date.

Our cash flow projections include the improvements to our underlying business performance as well as early benefit from our initiative to reduce pharmacy inventory in our retail stores by $1.5 billion in 2022. We continue to expect 2019 net capital expenditures of $2.3 billion to $2.6 billion.

In terms of the fourth quarter, there are a few things to keep in mind. For Health Care Benefits, the last quarter of the year is typically lowest adjusted operating income quarter due to the seasonality of the business including spending to support January 1 readiness for our Medicare business. Fourth quarter will also include higher sequential spending for our transformation programs.

Finally, given the timing of the close of the Aetna transaction, prior year fourth quarter does not include the full impact of share dilution and interest expense resulting from the transaction. These differences affect the year-over-year adjusted EPS comparability.

As we look ahead to 2020, we feel very good about the momentum in our business and we are even more confident in generating at least $7 of adjusted earnings per share with low single-digit growth off our 2019 baseline, which excludes the non-recurring items of approximately $0.20 I mentioned earlier. These items will not be included in our 2020 guidance consistent with the legacy Aetna practice.

As we have stated previously, we will provide full 2020 guidance on our fourth quarter earnings call. In summary, we continue to execute against our plan and we are confident that we will be able to achieve our financial and operating goal for the full year and over the longer-term.

We remain focused on strengthening our business to deliver sustainable long-term growth and create value for all stakeholders through our transformation into the most consumer-centric health company.

With that, I would like to open it up for your questions.

Question-and-Answer Session

Operator

Thank you. At this time, we will be conducting a question-and-answer session. [Operator Instructions] Your first question comes from the line of Lisa Gill with JPMorgan. Lisa, your line is open.

Lisa Gill

Great. Good morning, everyone. Larry, I want to start with your comments around the HealthHUBs. You talked about the outperformance versus the control group. I really have three questions here. One, any numbers that you can share around that? Two, as we think about the impact of rolling out another 50 this year and as we get into 2020 will it have any impact on your 2020 numbers?

And then thirdly, as we think about additional services that will go into the HealthHUBs, have you thought more about primary care versus episodic care. And as you think about that integrated model with the medical side, are you learning anything from those Aetna members of incremental services that you think you need to bring to the HealthHUB?

Larry Merlo

Yes, Lisa. Good morning. And I'll start and then I'll flip it over to Kevin. Yeah, Lisa in terms of the numbers themselves as you know we have been qualitative in our definition of performance, and we've done that, it's a very small subset of stores at this point.

But as you've heard us say countless times, it absolutely has given us the confidence in the belief in our strategy and the need for a rapid rollout. So, as we get more of a critical mass of stores, you will see us move from qualitative definition to more quantitative definition.

And you can think about that sometime in the – probably in the second quarter timeframe, in the spring time frame, where we think we'll have enough of a critical mass and multiple geographies across the country.

And Lisa, in terms of 2020 impact, as we've talked, the rollout will go through 2020 as well as 2021. And you really have two dynamics in play here. You've got gaining that critical mass of HealthHUBs as well as the opportunities for client adoption.

So, I do believe that that will take some time. I wouldn't expect that we will see a material impact in 2020. I think it's more 2021 that we'll see that happening. But again, we're extremely excited in terms of what we have seen and what we've learned in Houston, and I'll flip it over to Kevin to pick-up on that third question.

Kevin Hourican

Thanks, Larry. Good morning, Lisa. Thanks for the question. I'll just build on the second part of your question which was the services provided. The new wellness product that we've added to the front store continues to do well, including the products that we're selling in the sleep apnea space helping fill white space in an unmet consumer demand.

We're bullish on the MinuteClinic expanded services getting into chronic disease management in a more coordinated way. We believe it's in collaboration with primary care to answer your question in replacement of primary care.

In the pharmacy space, we're excited about what our pharmacists are doing in partnership with data coming to us from the Aetna business unit on which patients need our greatest help on a longitudinal way. So it's not one phone call and one specific day.

It's over a course of time working with those patients to help introduce them to care coordination services that are available through Aetna and also working with the PBM sales team on what the members of our Caremark business units are looking for.

And just an important point to note as it relates to your provider question, 80% of the services that can be provided by a primary care physician can in fact be provided by our nurse practitioners in our pharmacies – excuse me, in our MinuteClinics. And again, we view it as complementary to primary care.

Lisa Gill

Okay. And then just as a follow-up, you brought up Caremark, are you seeing either Jon or Karen, are you seeing anything as far as the selling season having an impact. I know Larry, it's still a small market.

But as we think about the number of MinuteClinics you have today, the services that you're providing, any impact at all in the 2020 selling season around having these offerings or again is that more of 2021? And I'll stop there. Thanks.

Karen Lynch

Hi, Lisa. It's, Karen. Yes, we've been – a couple of things on this topic. We've been talking to our clients throughout the 2020 selling season about how we can deliver that more personal, integrated, cost-effective, and holistic care approach -- response from our customers has been very positive to date. And I think we're seeing a fair amount of activity and pipeline build for 2021.

And as we talked about previously, our focus for 2020 was to go to market with a more integrated medical pharmacy offering, and what we've done for the 2020 selling season, I'm very pleased to tell you that we are seeing increased traction in overall pharmacy penetration for our employer sponsor business, particularly where Aetna had the medical business and we're now winning significantly greater percentage of pharmacy business. So there's a lot going on and we're – I can talk later relative to the – some of the pilots that we have but I'll let Jon cover where we're headed.

Derica Rice

Lisa this is Derica. In regards to you on the Caremark side, we've had the opportunity to introduce the HealthHUBs to a number of our clients both on the health plan side as well as on the employer side, and we've had a great deal of excitement and interest, and it's clearly playing out not only in our 2020 selling season, we look to wrap that up, but also to 2021.

And I know there was always – with the announcement of the deal between CVS and Aetna, there was some concern amongst investors about potential for channel conflict. We – with the interest that we have from some of the health plan clients, we've actually now listed two that are actually performing some pilots with us that was related to the HealthHUB itself. So that gives you some idea to the type of traction we're getting in that space.

Jonathan Roberts

And Lisa this is Jon. If you remember back when Caremark rolled out Maintenance Choice and the excitement in the market and the momentum that gave us, we're seeing a similar reaction in the market to HealthHUBs from the clients.

Lisa Gill

Thank you very much.

Jonathan Roberts

Thanks, Lisa.

Operator

Your next question comes from the line of Lance Wilkes with Sanford Bernstein. Lance your line is open.

Lance Wilkes

Yes. My question is on the PBM and it looks like a strong performance. I was wondering in 2019 how much cross-sale you're seeing in the Aetna book of business for this year as contrasted with maybe some sort of metric related to how much progress you're going to see for the beginning of 2020, given the selling season that Karen just mentioned. And then what do you see as sort of the upside possibility with that? And I guess related to the PBM also is for those additional wins you got over the last quarter, what segments are those in? Is that a health plan or employer business/

Karen Lynch

Lance it's Karen. Let me just talk about where I see the opportunities on PBM. As I mentioned, we're having a good 2020 selling season. And what we're measuring is really penetration of the book. So we're looking at a number of ways. We're looking at where we have medical and we want to drive pharmacy integration.

We're looking at the – Derica and I are jointly looking at the pharmacy book and looking at where we want to potentially sell medical opportunities. And then we're looking together holistically to say, 'Hey where are the opportunities that neither one of us have business? And that's where I think we're starting to see that growing pipeline in 2021 and bringing all the capabilities of the company together. And we've just recently had a lot of customer interactions, we've been out in the market with our brokers talking about this integrated story, and we are seeing very positive response.

Kevin Hourican

And Lance just to build upon Karen's comments. In regards to the impact on the PBM, you've seen here off the late that we -- at least since the Q2 call that we've improved our net wins by $1 billion. The vast majority of that came in the employer segment and call it the kind of the middle market and that plays very well with the integration efforts that Karen laid out also.

And then as you can think about what I talked about earlier about being able to introduce the HealthHUBs and some of the broad array of services to that client group, that's -- they've been very receptive to that and absolutely is playing into the outlook and the expectations we're establishing in the marketplace.

Lance Wilkes

Great. And just a quick follow-up. Karen, previously, you'd talked standalone Aetna about efforts in the kind of down-market employer segment to do more cross-selling, more bundled sales and kind of go after that self-insured market more. I'm just wondering what was the status of progress on that for you guys looking at 2020.

Karen Lynch

Yes. It's obviously early for 2020 for that end of the market. Now, we've been very focused on national account higher end of middle. So, it's a bit early, but we have the teams out talking about our new capabilities relative to the HealthHUBs which people are excited about. We've introduced our NovoLogix capabilities that people are introduced about. And then we're -- people are excited about our new digital capabilities. So, we are pushing our integrated message throughout all of our segments and we are seeing some good interest, but it's really too early to tell you about 2020 at this point.

Lance Wilkes

Okay. Thanks.

Larry Merlo

Next question.

Operator

Your next question comes from the line of Charles Rhyee with Cowen. Charles, your line is open.

Charles Rhyee

Yes. Hey thanks for taking the question. When I look at the full year guidance for the rest of this year, you kind of talked about year-to-date product development and net realized capital gains of $0.20. When we're thinking about next year and 2020 and sort of like when you initially kind of had said better than $7 a share, should we be looking at this number including the capital -- this kind of number assuming that we probably have similar types next year or should we be thinking about it without?

Eva Boratto

Yes, Charles, this is Eva. Thanks for the question. I think, as I outlined in my prepared remarks, right, where we're sitting today versus where we sat back in June, we're even more confident with our low single-digit growth. We provided the transparency and the color around the $0.20. As we've said consistently, we don't guide to that. So, think about that growth off -- after you remove that from your baseline.

Charles Rhyee

Okay. And is there any kind of -- as we think about the fourth quarter, is there -- I think, typically, prior period development is really more of a second and third quarter kind of impact typically. Is that -- would you expect more than anything in the fourth quarter?

Eva Boratto

Typically, Charles, as you think about the fourth quarter, there's de minimis prior year development if you look at historical patterns. We'll continue to provide the transparency on this and the realized capital gains as we go forward.

Charles Rhyee

Okay, that's helpful. If I could just sneak one other on the HealthHUB, going back to Lisa's question. You talked about 50 stores by year-end. 1,500 stores by 2021. Is there a good interim target as we think about 2020 number of stores?

Larry Merlo

Yeah. Hey, Charles, it's Larry. You can think about that, we'll probably be in the zip code next year of 600 to 650 stores by year-end.

Charles Rhyee

Okay. Awesome. Thank you so much.

Operator

Your next question comes from the line of Ricky Goldwasser with Morgan Stanley. Ricky, your line is open.

Ricky Goldwasser

Thank you and good morning. So firstly, just to clarify on the EPS guidance question. So Eva, if we think about the new 2019 base of $6.97 to $7.05, and we excluded $0.20, and we grow it by low single-digit, we get to a range of $6.84 to $7.12. I know that you answered before above $7. So should we think about would you say that you're comfortable with kind of like that high low single-digit range?

Eva Boratto

Yeah, Ricky, as we said, we'll provide our more fulsome guidance in February, but we've reiterated we're comfortable with at least $7 and the low single-digit growth, and we'll have more to provide…

Ricky Goldwasser

Okay. That's helpful. And then my question is focused on specialty. And Karen, maybe this one is for you. When we think about the opportunity in specialty, what's the specialty penetration within the Aetna book of business? And how do you think that kind of like growing over time?

Larry Merlo

Ricky let me just ask a point of clarification. When you're talking specialty, are you talking about specialty pharmacy or just the specialty businesses within Aetna that includes pharmacy and others?

Ricky Goldwasser

Specialty pharmacy.

Larry Merlo

So Ricky, as you know that's one of the highest-trending medical cost categories that we have. And we've been working very closely with Derica's team on managing those specialty drugs and that specialty costs. And we are introducing some new capabilities into the market relative to 2020. It's a critically important concern for our customers, particularly with the new drugs that are coming out that have very high cost. So we are looking at innovative capabilities around stop-loss potentially.

And again, we've introduced our NovoLogix capabilities across our portfolio, which I think will bring those costs -- we're hoping to bring those costs down and in line. So we're really excited. And as we've been talking to our customers they're excited about the possibilities there as well.

Karen Lynch

And Ricky just to emphasize the point that Karen was alluding to we would sit here today and say that there is a large portion of specialty that flows through the medical benefit that has been largely unmanaged and that becomes a big opportunity here.

Ricky Goldwasser

Yeah. And that's really where the question was what's the incremental opportunity, where you're currently not managing. And then if I may just one follow-up, because you talked about long-term care in Omnicare. How do you think about the progression of Omnicare first half versus second half? And how is it performing against your targets and kind of like that opportunity to have Omnicare being a positive -- contributing positively to next year.

Jonathan Roberts

Yeah, Ricky, this is Jon. So long-term care is performing slightly better than expected in 2019 and we've started to see improvement in our new sales and retention given our service improvements. And at the same time we also continue to improve our cost structure. I will say this market continues to be challenging as our clients have continued to divest facilities in 2019. And we'll have more to say about it on our fourth quarter call.

Ricky Goldwasser

Thank you.

Operator

Your next question comes from the line of Michael Cherny with Bank of America. Michael, your line is open.

Michael Cherny

Good morning, and thanks for taking the question. I want to dive a little bit into the retail TC segment particularly profit growth in particular. You pointed to a lot of the moving pieces in the quarter and where things shook out on the positive versus negative side. Also, I know at the Investor Day you did talk about that segment being up at least some preliminary expectations low single-digit on EBIT. I guess, based on what you've seen so far year-to-date, having just obviously addressed the long-term care question, how was everything tracking relative to the moving pieces within retail that will allow you to drive towards EBIT growth of that low single-digit rate into next year?

Eva Boratto

Hi, Michael. This is Eva. I'll start and perhaps Kevin will jump-in. As we look at Q3, Q3 performed right in line with our expectations. Q2 performed above our expectations. So we're pleased with how the business is performing and the initiatives which are underway to enable us to return to growth in the segment.

Kevin Hourican

I'll just build on that. Your second part was our confidence and not being able to hit the guidance that we provided back on Investor Day for 2020. As Eva just said, we're on track to be able to deliver against that guidance. In fact, we're more confident now than we were then. The key tenants of that strategy to enable that growth we'll grow our pharmacy business faster than the industry and continue to take market share and grow organically, which we've been doing this year and that will continue. We will continue to grow both the top line and bottom line within our pharmacy – excuse me, front store business, specific focus on health and beauty. The biggest year-over-year difference is a meaningful cost takeout through the modernization efforts that Jon Roberts covered back in June. Those efforts are on track. We will take a significant amount of cost out of both our pharmacy and front store businesses. Those three things working in concert will enable that low single-digit growth that we guided back in June.

Michael Cherny

Great. And then just one quick point of clarification to make sure we got this based on keeping the guide for the MBR it seems like there's a pretty implied high number for 4Q. Aside from seasonality, is there anything else that we should think about in there that drives that number higher than where it's been trending over the course of the year?

Eva Boratto

No, there's – Michael this is Eva again. There's nothing that we would call out.

Michael Cherny

Okay. Thanks so much.

Operator

Your next question comes from the line of George Hill with Deutsche Bank. George, your line is open.

George Hill

Yeah. Good morning, team CVS. And I kind of want to dovetail right off of Mike's question which is, I guess are you able to quantify maybe the cost takeout that you're looking for in retail pharmacy next year? And I guess just given – looking at the pharmacy results for this year. And I don't think there's any reason to think the reimbursement next year is going to meaningfully improve. I'm also just trying to bridge the gap between kind of putting the retail pharmacy results this year and how we get that low single-digit EBIT growth in the segment next year. So quantification on the cost takeouts and maybe the outlook for reimbursement or the year-over-year change in reimbursement and how it impacts results would be helpful. Thank you.

Larry Merlo

Yeah. George, it's Larry. Good morning. Maybe just a couple of things to be reminded of as we went through the first half of this year, keep in mind we have the additional investments that we made back in 2018 that cycled through the first half. Largely, the investments in tax reform as it rolled back into our retail business for our colleagues. And then George, I would take us back to the Analyst Day in terms of -- we provided the headwinds, tailwinds as we looked at next year. And there's nothing different that we see today from what we had talked about back in June. And as you pointed out, we don't see reimbursement pressure abating, but the offsets to that reimbursement pressure have some dynamics in 2020 that we did not face in 2019. When you look at the contribution of generics as one example.

George Hill

Okay. And maybe just a quick follow-up for Eva. On the PPD in the quarter was that -- and you kind of related that it was -- was it -- I guess was the positive PPD in the quarter was it in response to the cost pressure that you saw in Q2? Or is it separate from the cost pressure you saw in Q2?

Eva Boratto

No. I would say, overall we had about $0.04 of PYD prior year development as well as net realized capital gains in totality. And the development that we saw was across all of our four core businesses.

George Hill

Okay. All right. That's helpful. Thank you.

Operator

Your next question comes from the line of Ann Hynes with Mizuho Securities. Ann, your line is open.

Ann Hynes

Hi, good morning. Just going to the PBM, I know there was a lot of discussion earlier this year about the future of rebates and has become more quiet since the White House -- the rebate rule. But so could we assume when it comes to rebates, it's business as usual going forward. That would be my first question. And my second question is with the federal employees contract, it looks like you extended another year. Do you ever anticipate that going to full RFP. I guess what was the decision behind them, I guess keep on renewing it. So how do you view that contract going forward? Thanks.

Larry Merlo

Ann, good morning. I'll take your first question and flip it over to Derica. Ann your first question on rebates, look if you go back what the last year, 1.5 years the debate was roll the PBMs what happens to the rebate dollars. And as we sit here today I think the debate has now shifted not on the PBMs, but to the manufacturers in terms of why are the list prices what they are and the data has proven the value that PBMs have brought to the marketplace in terms of reducing the net price of pharmaceuticals through formulary management et cetera.

So we don't see that dynamic changing. And as a matter of fact, some of the various bills that are currently in committees today broaden the tools that have been proven to be successful for the PBMs in terms of introducing more competition across therapeutic classes to include biosimilars and some of the things that have delayed competition from entering the marketplace.

Derica Rice

Ann, this is Derica. We've been able to take advantage of that. And as we also shared back in June that we would be able to manage or rebate exposure very efficiently. And we've seen the peak this year. And in fact, we're doing slightly better than anticipated and that will mitigate over time and continue to dissipate as we think about 2020. And then to your second question regarding FEP along those lines we're very pleased that we were able to extend our relationship with them. We have a very strong partnership and history with FEP. I would anticipate at some point it will go to RFP, but the fact that we've been able to continue that relationship I think bodes very well for us and speaks very strongly to how we've been able to create a partnership that's lasted for a number of years.

Operator

Your next question comes from the line of Robert Jones with Goldman Sachs. Robert, your line is open.

Robert Jones

Great. Thanks for taking the questions. I guess just a couple of more detailed follow-ups. I mean one, Eva I think you mentioned a larger-than-expected benefit from generic launches, particularly in specialty. So I was just wondering if you could expand on that dynamic a little bit. And was this an area that you guys were expecting? Or is this actually something that could be trending more meaningfully in your favor as far as follow-on biologics or generic biologics?

Eva Boratto

So Bob I'll take the first part. I think Jon will provide some more color. Overall, the timing of the launches and when they come to market can vary. So this was something we were expecting albeit it came early for us. And as we continue to focus to execute and deliver value and savings right driving the penetration of generics is an important priority for us.

Jonathan Roberts

Bob, this is Jon. So for 2019 we continue to improve our purchasing economics on mature products. And then when they – we looked at some of the new generic launches that were coming to market, we actually were able to get more favorable rates than what we historically had. So that was a positive.

And then we had some new generic launches that we did not expect that were favorable. And then as we look forward into 2020 and beyond, we still see significant generic launches and launches of biosimilars. And between 2020 and 2023, there'll be $41 billion of generics and biosimilars that will come to the market.

And in addition to that we see opportunities to improve how we purchase complex generics, generics where there's only one manufacturer and also again a great opportunity around biosimilars. So we still see this as a very attractive area for us.

Robert Jones

Got it. And then just one quick follow-up maybe for Karen. We've gotten some questions on disclosure from WellCare related to Aetna's PDP. I think it generated around $300 million in gross profit in the first three quarters of this year. Is that the right way we should think about the impact to Aetna CVS, when that PDP business eventually rolls off next year?

Karen Lynch

So Bob, we haven't provided that level of detail on specific parts of the business. Obviously, there will be an earnings hit related to the roll-off of the business, as well as our need to work through some stranded costs Karen's team is focused on. And when we give guidance in February, we'll try to provide some more color.

Robert Jones

Okay. Great.

Operator

Your next question comes from the line of Ralph Giacobbe with Citi. Ralph, your line is open.

Ralph Giacobbe

Great. Thanks. Just wanted to go to Health Benefits segment. Obviously last quarter you had noted the pressure in commercial and middle markets in the specific geography. It sounds like you've made some improvements there. So if you can help with sort of the deals and what sort of got better. But at the same time you're still expecting MLR above midpoint. So maybe just help on that more broadly.

And then if you could just help us with cost trend by segment just commercial Medicare and Medicaid and within Medicaid. Specifically there's been a lot around reverification issues, we've heard from some of your peers. Is that hampering your margins in the segment? And is that driving up the MLR as well? Thanks.

Eva Boratto

So a lot of questions there. I'll start with the commercial medical cost question. Yes we mentioned in the second quarter that we had some pressure in utilization in our lower end of the middle market. During the second quarter, we noted that we took appropriate actions to address those elevated medical costs. And I would tell you with an additional three months of claims experience, we feel comfortable that the actions that we took have mitigated the elevated pressures that we thought we saw in the second quarter. Specifically, what we did was we had intensified our medical management in those geographies, the claims activity that we now have seen, we believe that we've identified the right products, the right segment and the right geographies where that business had what we thought was elevated utilization. We feel that we've effectively addressed it. Relative to medical cost by segment, we have not disclosed that. I'll let Eva take that question.

Larry Merlo

Yes. I think as you look -- listen, we've indicated all of our businesses are performing well. As you look at the mix of our business and its government has really grown, we look at the overall MBR as an indicator around the health of our business. The other thing that I would highlight is just recall SilverScript is now part of the MBR related to the healthcare benefits segment which is larger than the legacy Aetna PDP and it performs differently within the MBR essentially reverse of the typical managed care.

Karen Lynch

Yes. And just a follow-up, I think you were asking a question on Medicaid redetermination. They've always been and continue to be something that we monitor very closely. There's really two impacts on redeterminations. The first and most obvious one is enrollment. The second one is on experience. Both impacts have been and continue to be immaterial for us. But as I said, we closely monitor it. But it isn't having any material impact on our Medicaid business.

Larry Merlo

Okay. So, thanks Ralph. Amy, we'll take two more questions please.

Operator

Thank you. Your next question comes from the line of A.J. Rice with Credit Suisse. A.J., your line is open.

A.J. Rice

All right. Thanks. Hi everybody. First of all, just maybe get you guys at this point we've got more information about the lay of the land going into 2020 around the Medicare Advantage product offering and competitive offerings are visible to you. We're in the early stages of the open enrollment period. I know at the Investor Day you guys had said you thought you could grow above market even, obviously with the hip and other things coming back. Any updated thoughts on how that looks, how much geographic expansion things like that will drive your performance next year might be a general range on growth and enrollment in the business?

Karen Lynch

Hi A.J., its Karen. Let me just comment on the competitive landscape and what our go-to-market strategy is. As you know, and as you've seen, the competitive landscape appears to be competitive in 2020. However, as you have seen CMS is estimating market growth to be about 10%. We think it will be a little bit lower than that, but we are still optimistic that we can outpace our industry growth despite the headwinds. And we -- there's a couple of reasons why we're optimistic. One, I would just say, we continue our efforts around geographic expansion. We're at 81% of Medicare eligible. We continue to make investments in our growth and retention of our existing service areas. Our stars performance is incredibly helpful to helping us in our optimism relative to Medicare growth. We have -- we maintained our zero premium plans and we're the top health plan with respect to zero premium plans. We also had expansion of our DSIT markets. And we are also focused as I've mentioned at Investor Day of converting our PDP business as well as our commercial business as our commercial business ages into retirement age.

And we believe that we can be successful relative to all those factors. I also would comment A.J., that we have incorporated some of our new and differentiated capabilities at the combined company. So we are offering the HealthHUB in our Houston market. We have zero cost share benefit coverage in our MinuteClinics. We introduced our Healing Better program in select markets.

We also offered a fall prevention benefit that provides members with an annual allowance for fall safety items that that if you've curated by CVS. And then our over-the-counter benefits provide members with an allowance at our CVS retail stores. So, all those factors give us optimism that we will have above-industry growth.

A.J. Rice

All right. And maybe one quick follow-up on the Pharmacy Services. I know throughout this year you've talked about the investment you're making to helping Anthem stand up its IngenioRx. It sounds like perhaps there is -- that may swing to the positive. Is there any way to talk about the order of magnitude of that headwind that now becomes hopefully a little bit of a tailwind heading into 2020?

Derica Rice

Hi, A.J., this is Derica. We haven't quantified in terms of putting this specifics. What we've stated is that clearly 2019 at least the first half was an investment year for us as we were looking to stand up that business. Now that we are far into the implementation of IngenioRx, which has gone really, really very well. We obviously now have transitioned to operating costs many of those expenses. We do expect that it will – while, it will be investment this year. We will turn profitable in 2020. And that's what we've stated.

A.J. Rice

Okay. Thanks a lot.

Operator

Your final question comes from the line of Steven Valiquette with Barclays. Steven, your line is open.

Steven Valiquette

Thanks. Great. Good morning, everybody. So a lot of the juicy topics have been covered already. So I guess for us just for Medicaid obviously the Texas Star plus was pretty positive for the company. Is there any additional color you can provide on what you think drove some of your success there either qualitatively or quantitatively just in terms of your ability to analyze the full outcomes for yourself relative to the other players? Thanks.

Larry Merlo

Yeah. So thank you. And we're really excited about being awarded the Texas program. We believe that some of the reasons why we won, we really believe we had a compelling RFP response. We have very strong existing value-based provider contracts in Texas. We had a very unique partnership with Texi Healthy Home area age -- aging agencies. We made a commitment to the DNT plan. We offered our Texas HealthHUB in that we believe helped us and we believe that our NCQA ratings helped us as well.

Steven Valiquette

Okay. Appreciate the color. Thanks.

Larry Merlo

Thanks Steve. So look let me just wrap up. It's really hard to believe that at the end of the month, we're going to celebrate our first anniversary as one company. And I could not be more pleased and proud of the commitment and engagement of our nearly 300,000 colleagues all across the country.

And as you've heard us talk this morning, our integrated model is designed to drive higher engagement, enhancing access to high-quality health care and reduce costs and create better health outcomes. And ultimately, that's going to feel and accelerate our revenue and EPS growth over the long-term. And I think again as you heard this morning our entire organization is laser-focused on executing the plan that brings that strategy to life. So let me thank everyone for their time this morning and we'll talk to all of you soon.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.