Cigna Corp

Cigna grabs vital scale with $67bn deal for Express Scripts

Takeover of pharmacy benefits manager to provide clout when buying drugs and services

Payers are demanding change to cut costs, prompting deals like Cigna's purchase of Express Scripts © FT montage / AP / Bloomberg

David Crow in New York YESTERDAY

With its $67bn takeover of Express Scripts, health insurer Cigna is sending a signal that it will have to get bigger to deal with the most pressing malady of US healthcare: soaring costs.

Express Scripts was the last large independent pharmacy benefits manager, or PBM, which acts a middleman in negotiations between drugmakers and the payers — the employers, insurers, and government, which buy medicines in the US.

By buying the PBM, Cigna hopes to gain more scale so it can drive a harder bargain when buying drugs and services, not just from pharmaceutical companies, but also the doctors and hospitals that provide patient care.

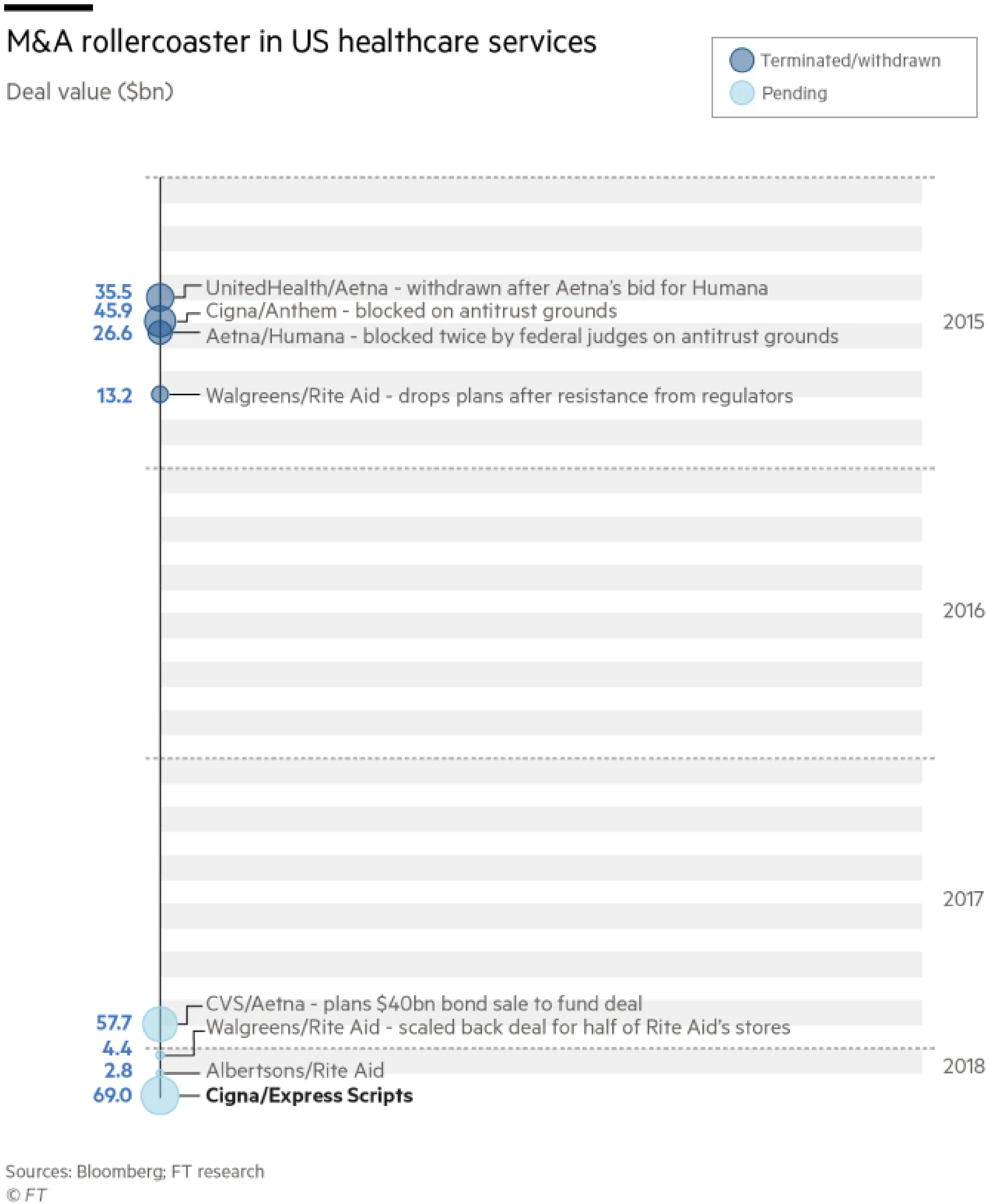
Since employers started funding healthcare during the second world war, the US system has fragmented into hundreds of for-profit companies, from insurers and private hospitals to blood-testing labs, pharmacies and drugmakers.

Although all these companies insist they put patients first, they also have a competing duty to provide shareholder returns, and all have benefited in different ways as US healthcare expenditure, adjusted for inflation, jumped from $221bn in 1960 to $3.4tn in 2016, growing on average 5 per cent annually over that period.

"The healthcare ecosystem puts tremendous pressure on our society, and by expansion on far too many individuals and families," said David Cordani, chief executive of Cigna, on an investor call on

Thursday, adding that the deal would make it "more affordable" for its customers to access care.

With total US health spending forecast to hit $5.7tn by 2026, large employers from Walmart to IBM have started to worry that spiralling costs will eat into their profits and are demanding change.



"The impetus behind this is that major corporates are really angry that insurance vendors like Cigna have been unable to contain the increase in costs," says Roger Longman, chief executive of Real Endpoints, a health analytics company.

"One of Cigna's points is that they'll have a lot more buying power after this deal," he adds.

That anger has prompted the formation of various alliances between large companies. Most recently Amazon announced it would start a new venture with JPMorgan and Berkshire Hathaway with a mission to lower costs.

And 40 large employers including American Express, Verizon and Coca-Cola have joined the Health Transformation Alliance, which is tasking the companies that provide healthcare to find ways to do more with less.

So far, the response of companies such as Cigna and CVS Healthcare — the drugstore chain that recently agreed to buy health insurer Aetna for $69bn — has been to get bigger through megadeals, arguing that consolidation will give them the power they need to push down costs.

Although the fragmented US healthcare system is still a far cry from the UK's National Health Service, these deals are at least in part designed to emulate some of the huge power wielded by "single payer" healthcare systems.

If a drugmaker wants to sell its medicines to patients in the UK, it must agree to sell those products at a price deemed acceptable by the country's powerful gatekeeper, the National Institute for Health and Care Excellence, or forgo those sales entirely.

More often than not, pharmaceutical companies agree to sell their drugs at a considerably lower price in the UK, but insurers such as Cigna and Aetna can only dream of having such power.

Drug costs, though, are only part of the problem: although spending on medicines has been rising well above inflation — especially for medicines prescribed by specialist doctors — drugs still only account for roughly 15 per cent of total healthcare costs.

A far bigger chunk of the cash — about 60 per cent — goes to doctors and private hospitals, which earn more when spending is high.

To tackle that part of healthcare spending, Mr Longman predicts that companies such as Cigna and UnitedHealthcare, the largest insurer, will start buying hospitals and clinics, and change their business models so they are incentivised to bring down costs.

One of the driving forces behind the CVS and Aetna deal was a plan to turn CVS's pharmacies into healthcare hubs, where Aetna's patients could be directed to receive low-cost care.

UnitedHealth has also moved into the “provider” sector, and in December spent $4.9bn on DaVita, which operates a network of clinics.

It is still unclear, however, whether antitrust regulators in the US will agree that the megadeals being pursued by Cigna and CVS really are necessary to lower costs.

Health insurers made much the same argument in 2015 when they tried to merge with each other in 2015 through big-ticket takeovers, but the Department of Justice blocked the deals.