

## Will Amazon Disrupt the Healthcare Industry?

*(Sources: an article prepared by Robert Langreth, Jared S Hopkins and Spencer Soper, with assistance from Zachary Tracer, and Naomi Kresge, & published by Bloomberg; a pharmpro.com editorial by Megan Parrish; an article by Dr. Adam Fein in the August 31, 2017 issue of Drug Channels)*

It is clear from the reports and rumors that have surfaced over the past 6 months that Amazon is exploring the possibility of entering the healthcare market. What is unclear, however, is how Amazon will enter the market, if it should choose to do so.

The prospect of the giant Internet retailer entering healthcare is beginning to cause far-reaching reverberations for a range of companies, impacting the shares of drugstore chains, drug distributors and pharmacy-benefit managers, and potentially precipitating one of the biggest corporate merger deals this year.

Just recently the pressure was plain to see. A report that Amazon had received pharmacy-wholesaler licenses in a dozen states triggered a fast and steep selloff that negatively impacted McKesson Corp., AmerisourceBergen Corp., and Cardinal Health Inc. Shares of Aetna Inc. surged after a Wall Street Journal report indicated that it's in talks to be taken over by CVS Health Corp. CVS and Aetna have held discussions about a potential deal, according to people familiar with the matter who asked not to be identified as the details aren't public.

Executives in the drug industry say that Amazon could use its expansive online reach and its logistical muscle to threaten companies that ship and sell medicines to consumers and cut pricing deals with drug makers. "Size and scale-wise, they can disrupt anywhere they want to disrupt," said Chip Davis, president of the Association for Accessible Medicines, a trade group for generic medication, in a recent interview.

A deal for Aetna could conceivably move CVS further away from the business of brick-and-mortar retail drugstores and deeper in health services such as pharmacy benefits, where it already has a sizable presence. Combining Aetna and CVS would create a health-services giant and a bigger competitor for UnitedHealth Group Inc., which is the largest U.S. health insurer and has its own clinics and a pharmacy-benefits unit.

The presence of Amazon is already being felt by retailers and companies that sell drugs over the counter. The head of Bayer AG's consumer-health business said on a conference call with analysts that the wider shift to online shopping by U.S. consumers was hurting its business. Erica Mann, the division's chief, dubbed it the "Amazon effect," saying buyers are looking for value.

At the same time, the hierarchy in the health-supply chain is beginning to shift. Analysts have speculated that Amazon could soon enter the business of selling prescription drugs, threatening to disrupt retail drugstores, drug wholesalers, and the pharmacy-benefits management business. While Amazon has never publicly commented on what its plans may be, the business news network,

## In Brief...

- ◆ **Cardinal Health** announced that *George Barrett* will step down as CEO and serve as Chairman. He will be replaced by current CFO *Mike Kaufmann* as of January 1, 2018, and the position of CFO will be assumed by *Jorge Gomez*. Cardinal also announced lower-than-expected quarterly revenue due in part to the low prices for generic drugs. The pharmaceutical unit made a profit of US\$467 million in the first quarter ended September 30th, a 13% drop year over year, but still ahead of analysts' expectations. **Cardinal Health Specialty Solutions** also introduced a new cloud-based patient engagement platform aimed at addressing an unmet need from the biopharma industry. The new platform will provide better insights into patient experience and the overall treatment journey.

- ◆ **McKesson Corporation** has signed a purchase agreement with **NRG Energy** for the construction of a new 3-megawatt solar installation at its Robbinsville, NJ distribution center location. Long term plans for solar arrays on McKesson distribution centers are included in the next phase of its sustainability program. Separately, McKesson announced that it has signed an agreement to purchase **RxCrossroads** from **CVS Health**. RxCrossroads is a provider of tailored services for

*(continued on page 2)*

*CNBC*, reported in October that the Internet giant could make a decision about selling drugs online by Thanksgiving. The network didn't name its sources.

*Bloomberg News* confirmed that Amazon had obtained wholesale-pharmacy licenses in at least 13 states, with an application pending in another state. Some of the licenses were obtained late last year and some this year. Speculation indicates that the licenses could be part of Amazon's business-to-business sales effort, which would include sales to hospitals, doctor's offices and dentists. Amazon recently announced "Business Prime Shipping," which brings the quick delivery associated with Amazon household orders to workplaces.

Amazon launched Amazon Business in 2015, offering tractor parts, latex gloves, file folders and millions of other products needed in factories, hospitals, schools and offices. Businesses are shifting their supply shopping online from less-efficient methods such as browsing print catalogs, faxing orders and telephoning sales representatives. Online business-to-business sales -- a broad category that includes pens and paper for the office as well as lab equipment and parts used in factories -- will grow to US\$1.2 trillion in 2021 from US\$889 billion this year, according to *Forrester Research Inc.*

On a conference call with analysts, McKesson CEO, John H. Hammergren, said the wholesaler doesn't "take the entry of any competitor lightly," but said the company already has a large online order operation and similar to what Amazon does logistically. "To some extent, we were Amazon before it was cool to be Amazon."

*(continued on page 2)*

## Amazon (cont.)...

After the news surfaced that Amazon might enter the drug space, analysts from Morgan Stanley issued a note explaining why they believe the change would be good for the pharmaceutical supply chain. “Establishing direct relationships with branded manufacturers, would be the most critical to changing the marketplace as we know it today, and could take a long time,” they wrote. “If Amazon were successful in changing the brand pricing model to be based on ‘net’ price versus the current gross model, we estimate a portion of rebates and other supply chain discounts currently being retained by plan sponsors, PBMs, and to a lesser degree drug distributors could pass back to consumers.” Many also believe that if there’s any distribution company that can navigate the complicated regulations around pharmaceutical sales and make it more efficient, it’s Amazon.

In the past year, Amazon has ramped up its hiring and consulted with dozens of people about a potential move into the pharmacy market. The consumables team, which includes groceries, kicked off the research, with the division's vice president, Eric French, taking the lead. It brought on Mark Lyons from Premera Blue Cross to build an internal pharmacy benefits manager for its own employees. Accordingly, it's possible that the push into the broader drug supply chain hinges on its success with this effort. In May, the company kicked off its search for a general manager to lead its pharmacy push, externally named "healthcare." Analyst firm, Leerink, has separately reported that Amazon will get into the pharmacy management space and expects an announcement within the next year or two.

Goldman Sachs published a report on the topic in August of this year, speculating that Amazon will ultimately look to improve price transparency for consumers and reduce out-of-pocket costs. Amazon already has a business selling medical supplies online, such as gauze and thermometers. It also has a health team called “1492”, which is focused on both hardware and software projects, such as developing health applications for the Echo and Dash Wand. Its cloud service, Amazon Web Services, continues to dominate the health and life sciences market.

Not so fast, says Dr. Adam Fein, President of Pembroke Consulting, Inc. and CEO of Drug Channels Institute, writing “Alas, our complex, Rube Goldberg–like drug distribution and reimbursement system is highly resistant to disruptive change...I would never underestimate Amazon. However, I believe that Amazon has limited feasible options for disrupting pharmacy and PBM markets... Here are some strategies that would likely be unsuccessful for Amazon: **Build or buy a PBM**... it’s clear that there are many complex services associated with administering a prescription drug benefit plan on behalf of an employer, health plan, or the government. The barriers to entry are just too high at this stage in the market’s evolution... There is also a trend toward greater pharmacy-medical integration and pharmacy-delivered patient care services. Amazon is woefully unprepared to compete in those areas.

**“Become a central-fill mail pharmacy in a third-party payer’s network.** Today, the largest mail pharmacies are owned and operated by PBMs and health plans. It is unlikely that these companies would allow Amazon to participate as a network mail pharmacy... The mail business is also not too healthy.

As QuintilesIMS reported recently, mail pharmacy is the only dispensing format that has experienced a sharp decline in the number of prescriptions dispensed. (Mail pharmacies, however, have significantly increased revenues, driven by the dispensing of specialty medications.) Retail pharmacies are accepting lower reimbursements to compete with mail pharmacies. Multiple states have enacted anti-mandatory mail order legislation that blocks plan sponsors from favoring mail pharmacies... And don’t forget that consumers report lower satisfaction with mail pharmacies compared with some other dispensing formats. Amazon would struggle to redefine this ultra-low margin business, assuming that PBMs would even let it participate.”

**“Build or buy a specialty pharmacy.** I also think it is also unlikely that Amazon can compete in the higher margin, higher touch business of dispensing specialty pharmaceuticals. A specialty pharmacy’s personalized and complex services are unlike Amazon’s highly scalable yet impersonal infrastructure. And even if Amazon could somehow overcome the barriers to participating in third-party payer networks, it would struggle to gain access to products in manufacturers’ limited dispensing networks.”

For more on Dr. Adam Fein’s August 31, 2017 article in Drug Channels please visit <http://www.drugchannels.net/2017/08/a-reality-check-on-amazons-pharmacy.html#more>

## In Brief (cont.)...

pharmaceutical and biotechnology manufacturers.

- ◆ In a move to push convenience for its patients, **CVS Health** will offer nationwide next-day prescription delivery and same-day delivery in selection cities beginning early next year, with Manhattan kicking off same day delivery on December 4th. Also included in the delivery service will be curated over-the-counter products. *Helen Foulkes*, CVS pharmacy president, said “Our goal is to meet the needs of all of our customers wherever, however and whenever they want. Providing same-and next-day options for delivery of medications is just another way we can help our patients get and stay healthy.” Cities slated for the same-day delivery rollout in 2018 include Miami, Boston, Philadelphia, San Francisco and Washington, DC.

- ◆ **Teva Pharmaceutical Industries Ltd.** (Israel) plans to set up a joint venture with **Guangzhou Pharmaceutical Holdings Ltd.** to make and sell Teva’s generic drugs.

- ◆ Swiss drug maker **Novartis** has agreed to buy French-based **Advanced Accelerator Applications** for US\$3.9 billion in a cash deal. The deal would give Novartis a platform in radiopharmaceuticals and strengthen its oncology business, as well as access to a cutting-edge therapy for a form of pancreatic cancer.

- ◆ **Allergan** reported third quarter earnings, topping expectations. The company also reported a double dip decline in revenue from its drug *Kybella*. Quarterly sales overall were up 11.4% to US \$4.03 billion, in line with analysts’ expectations. Revenue from the company’s blockbuster, *Restasis*, grew 2.9% to US\$366.8 billion, although Allergan now faces stiff competition from a number of generic versions of the drug.

(Sources: Bloomberg, Company Press Releases, Drug Store News, Marketwatch, and Reuters)