A tough pill to swallow
Pharmacy Benefit Managers must adopt a new model before time runs out
By Milind Pawar
Some of the most important players in the US healthcare industry are companies most people have either never heard of or do not completely understand. They are Pharmacy Benefit Managers (or PBMs), which work behind the scenes to administer the prescription drug benefit components of sponsored health plans for some 266 million consumers.¹

For decades, PBMs have served a vital role in the delivery of medicine. But over the past few years, the pressures of mergers and acquisitions, commoditization, shifting consumer expectations, and fast-changing health insurance dynamics have converged to call the very role PBMs play into question.

To survive the threat of disintermediation they now face, PBMs must establish a differentiated operating model—one focused on health outcomes, digitally enhanced experiences and operational excellence. The time to act is now.
On the fast track to irrelevance

PBMs are primarily responsible for processing and coordinating the delivery of prescription drugs and acting as intermediaries between payers and other value chain constituents such as pharmaceutical companies and government health programs.

In addition to developing and maintaining drug formularies, they perform the important job of ensuring that the medicines delivered are safe for consumption and won't react with other drugs that the patient may be taking. And with their size and purchasing power, they negotiate with pharmacies and drug manufacturers to lower the price of medicines.

A quick review of PBMs' historical performance or a scan of industry reports would suggest that PBMs are maintaining their relevance—and their profitability. This is especially true for the three PBMs that control 78 percent of the market. But there are clear signs that the capabilities and operating models that spurred PBM growth in the past won't work in the future. Why? Because most PBMs have been slow to adapt to the industry trends and market threats that are impacting their role in the ecosystem. If they don't take steps now to address these challenges, it is unlikely they will be able to retain their relevance in the years ahead.

In 2014, the PBM market was valued at $263 billion. By 2019, it is forecast to grow to $283 billion.
Fighting for the right to survive

At this point, no stand-alone PBM has developed a sustainable operating model that addresses the pending threat of disintermediation. Moreover, developing a new operating model takes time—a key variable that is not on PBMs’ side. PBMs must take action now to overcome the challenges they face:

Demand for new reimbursement models
The US healthcare industry is undergoing a dramatic shift from volume to value. Experts predict that the focus on value-based reimbursement is likely to remain even in the wake of the US Trump administration. Moreover, patient outcomes and constituent experiences now underpin many reimbursement models. In fact, by 2020, 75 percent of commercial payments may be made via value-based arrangements. Yet, PBMs continue to devote their energy and attention on reducing costs. Their incentives are not yet aligned to the outcomes the rest of the industry is pursuing.

Commoditization of services
PBM services have become more commoditized in recent years, opening the possibility that other players can step in to steal market share. Similarly, there is nothing particularly unique about the way PBMs deliver their services. Accenture research shows that the industry is moving toward hybrid models, in which Healthcare systems deliver integrated services to improve treatment efficacy and patient outcomes. Insurers and employers are already exploring whether they can assume the role that PBMs have played for their stakeholders. While 85 percent of Fortune 500 employers now use PBMs in carve-out arrangements, it is likely that many of these arrangements will be replaced with capabilities that payers build in-house.
**Industry mergers and acquisitions**

M&A activity in the insurance industry is creating ever-larger organizations with ever-greater leverage over PBM contract terms, fees and conditions. Recently proposed alliances between the top four payers is a good sign of additional consolidation of power. PBMs must now defend their value proposition—something that is difficult to do for organizations whose services are no longer differentiating. To compete, PBMs must interact more directly with end customers and consumers. And they must extend their constituent base to encompass other large employers.

**Demand for digital experiences**

Digital is now widely embraced as a critical tool for driving efficiencies and improving the quality of care. Insurers are flocking to the use of personalized technologies to monitor drug adherence and improve the health of their patients. The use of personalized health apps and wearables has doubled in just the past two years. Seventy percent of health executives are investing more in embedded artificial intelligence solutions. Specialty drug makers and digital medicine companies are also using digital to make personalized medicine a reality. Yet, for PBMs, it is largely "business as usual" because the best consumer experience requires integration of information across PBMs and payers.

**Greater industry focus on quality outcomes**

Like all consumers in the digital age, PBM constituents are more demanding than ever. They want more than an intermediary that can help reduce costs. They want a true partner to help them deliver better outcomes. For the reasons cited above, PBMs are not meeting expectations. As just one indicator of this, overall patient satisfaction across the PBM experience ranges from 65 to 75 percent. That’s hardly a ringing endorsement.

**Big is (not necessarily) better**

Consolidation among smaller PBMs is on the rise. So are collaborations between PBMs and pharmacy chains. Many industry-watchers believe those latter deals will raise drug prices. That poses a big problem. Prescription drug costs already make up nearly 10 percent of healthcare spending in the United States. With the advent of more specialty drugs, this percentage will surely rise. As the entire industry looks for ways to reduce costs, PBMs will be in the spotlight. If they are no longer able to keep a lid on drug prices as they have in the past, the value they deliver to the payer community will be significantly diminished.
Don't treat the symptoms. Cure the disease.

It’s clear that the traditional operating models PBMs have employed no longer align to the needs of today’s healthcare environment. Unfortunately, the challenges PBMs face will become more pronounced.

The good news is that those that act now can redefine the role they play in the healthcare ecosystem with a differentiated operating model—one focused on health outcomes, digitally enhanced experiences and operational excellence. To launch this multi-year transition towards a new-age model, PBMs should embrace five imperatives.

**Become outcome champions**

Rather than just distributing pills, PBMs of the future will focus on building capabilities that allow them to contribute more meaningfully to positive patient outcomes. This means flexing their innovation muscles, collaborating with other industry players to improve drug delivery, efficacy and adherence, and improving direct patient engagement by understanding and addressing their needs in a more personalized manner.

**Redefine their worth**

The healthcare system is rapidly shifting toward value-based payment systems. Yet, PBMs continue to expect payments based on transaction volume. Those that launch a value-based reimbursement strategy early will not only attract more payers and employers, but also set the payment model for the entire PBM sector.

**Be disruptive**

To stave off disintermediation, PBMs of the future will disrupt payers by getting closer to employees and consumers. Pharmacies have succeeded in this space by launching loyalty programs. PBMs should follow their lead.

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**The untapped digital opportunity**

Proteus Digital Health has developed an ingestible sensor that can be embedded in tablets to digitally record ingestion. This sort of advance fundamentally changes how healthcare providers can treat their patients. PBMs, however, have been quite slow in understanding how they, too, can use digital to build on the innovations of others or improve the experiences of their constituents.
Architect new—and more valuable—experiences

Winning PBMs will embrace digital opportunities to deliver experiences that their constituents now want and expect. This means understanding how payers, providers and drug manufacturers are using digital to improve patient outcomes and then identifying opportunities through which they can augment and differentiate those efforts. It also means using digital not only to streamline their billing, processing and delivery processes, but also to provide the transparency that the healthcare industry now requires.

Form unconventional partnerships

PBMs of the future will partner with others in “ecosystems” to drive operational efficiencies and provide more or differentiated constituent experiences than they might be able to provide on their own. For example, collaborations with non-traditional players like Amazon or Uber could help speed and streamline PBMs’ drug delivery service.

Deliver more than medicine. Deliver value.

Despite the dramatic changes that have taken place in the US healthcare market in recent years, PBMs have largely retained a status quo approach to the services they deliver. Their inaction would be acceptable if their traditional approaches aligned to the realities of today’s healthcare environment. But they don’t.

PBMs now have the chance to redefine the role they will play by crafting a new-age model operating model that will help enable them to deliver services in a different—and differentiated—way. PBMs that focus on improving patient outcomes, operational efficiencies, and the experiences constituents demand will not only reclaim their relevance, but also position themselves as much more valuable members of an integrated healthcare ecosystem.
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Notes

1. Pharmaceutical Care Management Association (PCMA), “That’s what PBMs do.”