

The cost plus healthcare revolution: why smart money is betting against margins and why we are seeing Andreessen create companies attacking cost plus models in cell and gene therapy

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ABSTRACT

Cost plus business models are experiencing a renaissance in healthcare, catalyzed by Mark Cuban's Cost Plus Drug Company and now expanding into new verticals including cell and gene therapy with Aradigm's recent launch. This essay examines why venture capitalists including Andreessen Horowitz and First Cressey Ventures are backing margin-compressing business models, the structural market dynamics that make these investments attractive despite lower gross margins, and identifies untapped healthcare segments ripe for cost plus disruption. Key themes include the strategic timing of Cuban's market entry, the unit economics that make cost plus models venture-backable, and specific opportunities in medical devices, specialty

pharmacy, and healthcare services where opacity and intermediary rent-seeking investable disruption potential.

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The Cuban Catalyst: Perfect Timing Meets Market Frustration

Mark Cuban launched Cost Plus Drug Company in January 2022 at basically the perfect moment in American healthcare's ongoing identity crisis. The timing was lucky, it was strategic as hell. You had a decade plus of mounting public anger at drug prices, Bernie Sanders making pharmaceutical pricing a mainstream political issue instead of just a wonky healthcare policy debate, and the pandemic had just put healthcare access and affordability on everyone's mind in a way that hadn't happened since the original Obamacare fights. Cuban walked into a market where the villain was already clearly identified, the pharmacy benefit managers and their opaque schemes and spread pricing models, and he offered something beautifully simple: we'll sell you drugs at our cost plus fifteen percent and a flat pharmacy fee.

The brilliance wasn't just in the model itself but in how it communicated value. Most healthcare startups spend years trying to explain what they do and why anyone should care. Cuban's pitch fit in a tweet and immediately made sense to anyone who'd ever looked at a prescription drug bill and wondered why their generic medication

somehow cost two hundred bucks. The transparency was the product as much as drugs themselves. You could literally see the acquisition cost, the markup, and the pharmacy fee broken out line by line on the website. It was almost insultingly simple, which is exactly why it worked.

But here's what made the timing really perfect: Cuban launched right as the FTC was starting to seriously investigate PBM practices and right before the Inflation Reduction Act would create even more pressure on drug pricing. He essentially rode a regulatory wave that was already building. The company didn't need to convince policymakers that drug pricing was broken, they already knew. It didn't need to convince the public that PBMs were adding cost without value, people were already furious about that. It just needed to exist as a working alternative at exactly the moment when the old system's defenders were most vulnerable to attack.

The other piece of perfect timing was the maturation of direct to consumer health and the regulatory environment around online pharmacy. Ten years earlier, Cost Plus would have faced massive friction around online prescribing, pharmacy licensure across states, and consumer comfort with buying medications online. By 2022, all those barriers had been largely solved by the telehealth boom during COVID and the general normalization of buying everything from razors to contacts online. The infrastructure and consumer behavior had evolved to make the model viable in a way that wouldn't have been true even five years earlier.

What Cuban proved was that you could build a venture scale business by just being radically transparent and fair in a market segment where opacity and unfairness were the default. That insight is now spreading to other corners of healthcare where similar dynamics exist, and that's where things get really interesting for investors who understand what he actually did versus what it looked like he did.

The Aradigm Model: Cost Plus Meets Cell and Gene Therapy

So Aradigm comes out of stealth in December 2024 with backing from Andreessen Horowitz and Frist Cressey Ventures, which is a pretty serious pedigree for a company.

attacking one of the hardest problems in healthcare financing: how do you make million dollar one time cell and gene therapies economically viable for health plans and health systems without bankrupting either the payers or the manufacturers. The answer is essentially Cost Plus but for the most expensive category of therapeutic that exists.

The cell and gene therapy market is fascinating because it's simultaneously the frontier of medicine and a complete financing disaster. You've got these incredible treatments that can literally cure diseases that were previously untreatable, but the upfront costs are so astronomical that even large health systems struggle to absorb them without destroying their operating margins. A single patient getting CAR-T therapy can represent millions in expense, and the negotiation between manufacturers, payers, and providers turns into this insane game of chicken where everyone's trying to risk to someone else.

What Aradigm is proposing, based on the limited information that's public so far, is to sit in the middle of that negotiation and essentially provide financing and risk management while taking a transparent markup instead of the traditional opaque pricing that characterizes specialty pharmacy and specialty therapeutics distribution. They're betting that they can make money by making the transaction more efficient and predictable for all parties rather than by maximizing information asymmetry and negotiating leverage like traditional specialty distributors do.

The really clever part is that they're entering this market right as cell and gene therapies are moving from ultra rare diseases into more common conditions. The first generation of CAR-T therapies treated diseases affecting thousands of patients. The next generation will treat diseases affecting hundreds of thousands or millions. This scale shift completely changes the economics and the risk profile for payers. When you're a health plan with five million members and you might see three CAR-T cases a year, you can kind of deal with that through reinsurance and stop loss. When you might see three hundred cases a year, you need a completely different approach to financing and risk management.

Aradigm is also benefiting from the same regulatory and political environment that helped Cost Plus Drug Company. There's massive pressure on cell and gene therapy manufacturers to figure out alternative payment models and outcomes based contracting because the current system of just charging two or three million dollars upfront is clearly unsustainable as these therapies become more common. CMS is pushing for it, private payers are demanding it, and manufacturers know they need to figure this out or face either regulatory intervention or market rejection.

The Andreessen Horowitz backing is particularly interesting because they're not traditionally a huge healthcare investor compared to some of the dedicated health funds. When they do invest in healthcare, it tends to be in things that look more like tech platforms than traditional healthcare services companies. That suggests the Aradigm as building infrastructure and technology for managing complex payment flows and risk rather than just being a specialty distributor with better unit economics. The Frist Cressey involvement makes sense because they're a dedicated healthcare private equity and venture firm that deeply understands provider economics and payer dynamics.

The question for investors is whether this model is defensible and scalable or whether it's just going to get competed away by existing specialty pharmacies and distributors who decide to offer more transparent pricing. My guess is that Aradigm is better off building proprietary technology for outcomes tracking, payment management, and risk modeling that makes them more than just a low margin distributor. If they're competing on price transparency, that's probably not a venture scale outcome. If they're building the financial infrastructure layer for cell and gene therapy adoption, that could be huge.

The Paradox of Investor Interest in Margin Compression

Here's the thing that confuses people about cost plus models: they explicitly reduce gross margins compared to traditional models, so why would venture capitalists, who generally love high margin businesses, want to invest in them. The answer is that

gross margin percentage is only one variable in the unit economics equation, and sometimes a lower percentage margin on a much larger volume at much faster growth rates with better capital efficiency produces a way better return profile than a high margin niche business.

Cost Plus Drug Company is reportedly doing somewhere in the range of several hundred million in revenue with extremely lean operations. The gross margin or fifteen percent markup is obviously lower than what traditional pharmacies make, but the customer acquisition cost is way lower because the value proposition sells itself; the lifetime value is higher because customer satisfaction and retention are through the roof, and the capital efficiency is better because you're not supporting a bunch of middleman infrastructure. The business doesn't need a huge sales force or expensive marketing or complex contracting because the product is the pitch.

Traditional pharmaceutical distribution has gross margins that look better on paper but requires massive infrastructure, carries significant regulatory and compliance overhead, and operates in a market where your actual unit economics per customer are hard to measure because of all the rebates and spread pricing and clawbacks. A seemingly high margin business that requires a ton of capital and overhead to operate can easily be less attractive than a lower margin business with clean unit economics and predictable cash flows.

The other piece that makes these models attractive is that they're often entering markets where the incumbents are earning rents through complexity and opacity rather than through actual value creation. When you strip out that rent seeking behavior and offer genuine value at a fair price, you can often capture market share way faster than a traditional competitor could. Cost Plus didn't need to compete in the traditional pharmacy battlegrounds of convenient locations or formulary placement or rebate negotiations. It just needed to be radically cheaper and more transparent than the alternatives, and it could grow almost entirely through word of mouth and organic demand.

Investors are also betting that once you establish a transparent, fair pricing model in one vertical, you can potentially extend that brand and that trust into adjacent

categories. Cost Plus started with generic drugs but could theoretically expand into other categories of healthcare products where similar pricing dynamics exist. The customer relationship and the trust you build by being genuinely fair and transparent in one transaction potentially unlocks opportunities in other areas where that trust is valuable.

The venture math also works differently when you're going after genuinely large markets with broken economics. If you're competing in a market that's efficient and functional, you need to have dramatically better technology or business model innovation to win. If you're competing in a market that's deeply dysfunctional and where the incumbents are widely disliked, you can win just by being normal and better. The total addressable market for prescription drugs in the US is something like \$400 billion annually. Even capturing a small single digit percentage of that with decent unit economics is a venture scale outcome.

Why the Smart Money Is Actually Smart Here

The investors backing companies like Aradigm understand something subtle about healthcare disruption that a lot of people miss: the biggest opportunities often aren't in inventing new technologies or capabilities, they're in fixing broken market structures and misaligned incentives. Healthcare is full of places where the value chain has been captured by intermediaries who extract rents without creating proportional value, and those are often easier to disrupt than markets where you need genuine innovation.

Frist Cressey and Andreessen Horowitz backing Aradigm is a signal that they think cell and gene therapy financing is one of those broken market structures. The current system has manufacturers trying to recoup massive R&D costs through astronomical upfront prices, payers trying to avoid financial risk by restricting access or demanding massive discounts, providers caught in the middle without the capital or risk appetite to take on these therapies, and patients either getting denied access or facing financial

catastrophe. Nobody is happy with how this works, which means there's a big opportunity for someone who can make the market function better.

The smart money is also betting on regulatory tailwinds. The political and regulatory environment is increasingly hostile to healthcare rent seeking and price gouging. We're seeing this with the FTC going after PBM practices, CMS pushing for transparency in hospital pricing and drug costs, and generally way more scrutiny of healthcare middlemen who can't articulate what value they're adding. Cost plus models benefit from that environment because they're inherently aligned with what regulators and politicians say they want: transparent pricing, fair markups, and reduced intermediary costs.

There's also a defensive dynamic at play. If you're a healthcare focused VC and you believe that cost plus models are going to disrupt significant parts of the healthcare economy, you basically need to have exposure to that trend even if the individual company risk profile is higher or the margin structure is less attractive than traditional healthcare investments. Nobody wants to be the fund that completely missed the cost plus wave because they were too focused on optimizing for gross margin percentages.

The unit economics can also be surprisingly good when you dig into the details. Aradigm is playing in a market where the average transaction size is potentially millions of dollars. Even with relatively thin margins, the absolute dollar contribution per transaction can be significant. If your average deal is facilitating a two million dollar cell therapy and you're making a transparent five or ten percent, that's a hundred or two hundred thousand dollars of contribution margin per transaction. You don't need that many transactions to build a real business, especially if your operating costs are relatively fixed and your sales cycle gets more efficient as you track record and credibility.

The venture returns can also come from being acquired by strategics who want the capability and the market position rather than from traditional exit multiples. A company like Aradigm could be extremely valuable to a large health system, a managed payer, or even a cell and gene therapy manufacturer who wants to own the financial

and distribution infrastructure for their own strategic reasons. The acquirer might not be valuing it on traditional revenue multiples but on strategic value and defensive positioning.

The Next Frontiers for Cost Plus Healthcare Models

So if cost plus is working for prescription drugs and potentially for cell and gene therapies, where else could this model create venture scale opportunities. I think there are several healthcare categories that have similar characteristics: opaque pricing, significant intermediary rent seeking, widespread customer dissatisfaction and large total addressable markets.

Medical devices and durable medical equipment is an obvious one. The pricing of things like wheelchairs, prosthetics, CPAP machines, and other DME is absolutely insane when you look at what Medicare pays versus what the actual manufacturing cost is. There are layers of distributors and suppliers all taking cuts, and the end result is that a wheelchair that probably costs a few hundred dollars to manufacture gets billed at several thousand. Insurance covers most of it so patients don't always pay the cost, but it's still a massive inefficiency in the system. A cost plus DME company that worked directly with manufacturers and sold at transparent prices could probably undercut traditional suppliers by fifty percent and still make money.

The challenge with DME is that a lot of the market runs through Medicare and insurance, so you need to either be willing to be out of network or navigate the complexities of becoming an in network supplier. But there's definitely a market for people who are willing to pay cash for DME if the cash price is actually reasonable and you could potentially build enough volume and credibility to eventually negotiate favorable in network rates. There's also an opportunity in the intersection of DME and consumer health products where the line between medical device and consumer product is blurry, things like hearing aids, continuous glucose monitors for wellness use, sleep apnea devices, and other products where a direct to consumer transparent pricing model could work.

Specialty pharmacy outside of cell and gene therapy is another obvious target. The whole specialty pharmacy market is characterized by crazy complex pricing, huge markups, lots of intermediaries taking cuts, and patients often getting crushed by cost sharing even when they have insurance. A cost plus specialty pharmacy that focuses on high cost oral oncolytics, HIV medications, multiple sclerosis drugs, and other expensive specialty medications could probably build a significant business by being radically more affordable and transparent than traditional specialty pharmacies.

The regulatory hurdles are higher than for traditional pharmacy because specialty medications often require special handling, patient management services, and close coordination with physicians, but those barriers also create defensibility once you build the capability. The other advantage is that specialty pharmacy patients are highly motivated to find savings because even with insurance their cost sharing can be thousands of dollars per month. They'll jump through hoops to save money, which reduces customer acquisition costs.

Clinical laboratory testing is another area ripe for cost plus disruption. The price for lab tests is absolutely wild, with the cash price at a traditional lab often being 10 or ten times what Medicare pays and sometimes a hundred times the actual cost of running the test. Quest and LabCorp have essentially duopoly pricing power in many markets, and they use it. There have been some attempts at transparent pricing like LabCorp's LabSight but none have really scaled to venture scale outcomes yet. The challenge is that most lab testing is ordered by physicians and paid for by insurance, so the patient isn't usually price shopping. But there's a growing market of direct to consumer lab testing for wellness and prevention, and there's also an opportunity in the uninsured and high deductible plan market where people are paying cash for labs.

The unit economics could be really attractive because the actual cost of running common lab tests is pennies to a few dollars, but the list prices are often fifty to several hundred dollars. Even selling at a small markup over actual cost, you'd be radically cheaper than incumbents. The challenge is building the logistics and infrastructure for sample collection and processing, but that's solvable with enough capital and operational focus.

Imaging services, particularly outpatient MRI and CT scans, are another category where pricing is opaque and wildly variable. The same MRI that costs three thousand dollars at a hospital might cost five hundred at an independent imaging center, but patients often don't know that or have easy ways to price shop. A cost plus imaging network that published transparent prices and made it easy to book and pay could capture significant market share, especially among the uninsured and underinsured population. The capital requirements are higher because you need to own or lease imaging equipment, but the unit economics are strong once you have utilization.

Medical supplies and consumables for clinics and medical practices is less sexy but potentially huge. Physicians and practice managers routinely complain about how expensive and opaque the pricing is for basic medical supplies, examination gloves, bandages, syringes, medications for in office use, all the stuff that medical practices need to operate. There are incumbent distributors like McKesson and Cardinal Health that dominate the market, but their pricing is often negotiated and variable, and smaller practices don't have much leverage. A cost plus medical supply company modeled after something like Costco for medical practices could be very attractive to small and mid size practices that are tired of getting gouged on supplies.

Outpatient surgery centers and procedural services could also work with a cost plus model, though this gets more complex because you're dealing with facility costs and physician fees, not just product pricing. But the core idea of transparent, fair pricing for common outpatient procedures is compelling. The Surgery Center of Oklahoma has been doing something like this for years, publishing their prices online and accepting cash payment at rates far below what traditional hospitals charge. They have been profitable and growing, which suggests the model works. Scaling it and adding venture capital to expand nationally could create a significant business.

Physical therapy, occupational therapy, and other outpatient rehab services are another category where pricing is opaque and often very high relative to the actual cost of delivering the service. Insurance reimbursement for PT is often pretty good, but most PTs charge whatever insurance will pay rather than competing on price. But there's a big market of people with high deductible plans or no coverage who need PT and are getting crushed by out of network rates of two hundred plus per session.

cost plus PT model that charged a transparent fair price, maybe seventy five or a hundred bucks per session, could probably fill capacity easily and build a nice business. The challenge is that PT is very local and relationship driven, so scaling requires either a franchise model or a very efficient playbook for opening and operating clinics.

Mental health services, particularly therapy and counseling, could benefit from a cost plus approach. The cash pay market for therapy is huge because insurance coverage for mental health is often inadequate and the reimbursement rates are so low that many therapists don't take insurance. But cash pay rates have gotten completely out of hand in many markets, with therapists charging two hundred to three hundred dollars per session or more. A cost plus teletherapy or in person therapy model that paid therapists fairly and charged patients a transparent reasonable rate could scale nationally. The unit economics work because the marginal cost of adding another patient to a therapist's schedule is basically zero once you've covered the therapist's time and overhead.

Picking Your Battles: Where Cost Plus Works and Where It Doesn't

Not every healthcare category is suitable for cost plus disruption, and it's worth thinking about what characteristics make a market attractive for this approach and where it's likely to fail. The best opportunities share several features.

First, there needs to be significant existing price opacity and wide variation in what different customers pay for the same product or service. If pricing is already transparent and competitive, there's no advantage to being cost plus. The whole proposition depends on being radically more transparent and fair than incumbents.

Second, the product or service needs to be relatively standardized and commoditized. Cost plus works great for generic drugs because amoxicillin is amoxicillin regardless of who sells it. It works less well for highly differentiated services where quality and provider expertise vary significantly. You can't really do cost plus for complex services.

procedures where the skill of the surgeon matters enormously because you're not competing on price, you're competing on outcomes and expertise.

Third, there needs to be significant customer pain around current pricing. People need to be actively unhappy with what they're paying and motivated to seek alternatives. If customers are satisfied or if insurance is covering the cost so they are not price sensitive, the cost plus value proposition doesn't resonate. The sweet spot is products and services where patients are paying out of pocket or have high cost sharing and feel like they're getting ripped off.

Fourth, the economics need to support relatively thin margins while still generating acceptable returns. This means either very high volume potential or high absolute transaction values where even a small percentage margin generates meaningful dollars. You probably can't build a venture scale business on cost plus bandages because the transaction values are too low. But you can build one on cost plus specialty drugs or medical devices where the unit economics are strong even with transparent pricing.

Fifth, and this is critical, there needs to be a path to customer acquisition that does not require massive sales and marketing spend. The whole advantage of cost plus is supposed to be capital efficiency and clean unit economics. If you need to spend hundreds of dollars in customer acquisition cost to get each customer, you've lost the plot. The best cost plus opportunities are ones where the value proposition is so compelling that word of mouth and organic growth can drive significant adoption at least in the early stages.

Where cost plus probably doesn't work well is in categories where clinical judgment and expertise are central to the value proposition, where customers are not price sensitive because of insurance coverage, where the regulatory barriers are so high you can't operate efficiently at scale, or where incumbents have genuine economies of scale or network effects that make it hard to compete on cost alone.

The other consideration is that cost plus models often start by serving the uninsured and underinsured market but need to eventually figure out how to work with

insurance to reach true scale. That means navigating the complexities of becoming a network provider, which can be challenging and expensive. Some cost plus companies deliberately stay out of networks to maintain pricing freedom and simplicity, but that limits total addressable market. Others bite the bullet and go through the process of contracting with payers, but then they're back in the weeds negotiating rates and rebates and all the complexity they were trying to avoid.

For angel investors and early stage VCs evaluating cost plus opportunities, the key questions are whether the market is genuinely broken and ready for disruption, whether the company has a credible path to customer acquisition at reasonable cost, whether the unit economics support venture scale returns even with thin margins, and whether the founding team has the operational excellence to execute a model that depends on efficiency and scale. Cost plus sounds simple in concept but it's actually very hard to execute well because you have no margin for error, literally. You need to be incredibly disciplined about costs and operations because you can't make up for inefficiency by just charging more.

The other thing to watch for is whether the company is actually committed to the cost plus model or whether it's just marketing language and they're going to gradually drift toward traditional pricing as they scale. True cost plus requires a level of transparency and commitment to fair pricing that needs to be baked into the company's culture and governance, not just the initial go to market strategy. If management starts talking about optimizing margins or competitive pricing instead of staying committed to cost plus, that's a red flag that they're losing the thread of what made the model attractive in the first place.

The best cost plus investments are probably going to be in categories where the current pricing is egregiously unfair and where a new entrant can demonstrate dramatically better value while still making attractive returns. Cell and gene therapy, financing with Aradigm, medical devices and DME, specialty pharmacy, lab testing, and outpatient procedures all fit that profile. The worst investments would be in categories where pricing is already competitive, where the service is highly differentiated, or where the unit economics don't support the operational requirements of a cost plus model.

What's clear is that cost plus is not just a fad or a one off success with Cost Plus Company. It's a genuine approach to healthcare disruption that works in market where opacity and rent seeking have created opportunities for transparent, fair pricing to win. The challenge for entrepreneurs and investors is picking the right battles and executing with the operational discipline that thin margin businesses require. But for those who get it right, there are probably multiple venture scale opportunities in bringing cost plus economics to broken healthcare markets.



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Mick Hayman  Dec 11

Interesting perspective. The cost-plus wave is on, but it's not the answer. It sounds good, like you're not getting ripped off.

Consider MA with its MLR restrictions. You have a cost-plus model, and it felt great. Insurers couldn't take home more than a set margin. Fast forward to the real world that we've lost the governor and the owner of the "plus" (margin) no longer has an incentive to manage the "cost" piece. And now where are we looking? Through the lens of and at physician salaries, site neutral payments, etc.

So, I want to own the "cost" piece in a cost-plus movement, at least for a few chaotic years. The end product simply "costs what it costs."



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