Merger Mania Accelerates

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MERGER MANIA HAS accelerated in the healthcare market, and pharmacy is a key factor driving these new alignments. Recent mergers that have caught our eye include:

- CVS/Aetna
- CIGNA/Express Scripts
- Albertsons/ Rite Aid
- Walmart/Humana

All sectors of the pharmacy market are impacted by these proposed mergers. Whether we are employees of one of these companies, submit claims to the PBMs (pharmacy benefit managers) or health plans, or have our insurance coverage from one of these healthcare giants, we will be directly affected by the new business models and alliances being created. Three out of four (exception: Albertsons/ Rite Aid) of these mergers are vertical integration plays that will influence the supply chain, concentrating power in larger organizations. As this column is written, the Federal Trade Commission (FTC) has not approved or challenged these mergers. A key dynamic, in our opinion, will be the expanded data pool for these organizations to mine and make better, more informed decisions for themselves and, hopefully, their patients.

All of these mergers forecast administrative costs savings by consolidating office functions — i.e., you don't need two accounting departments. Assuming these corporate giants can decide on a single administrative location, headquarters, etc., there will be millions or billions saved by reducing overhead. Let us look at these mergers in greater detail by grouping these new mega-entities by business type and examine the impact on pharmacy.

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VERTICAL INTEGRATION: RETAILER ACQUIRING AN INSURER

CVS/Aetna and Walmart/ Humana

Both CVS and Walmart are purchasing a health insurance company with the expectation that the retailer would gain a preferred pharmacy network position for patients to obtain their prescriptions. CVS drives 70% of its retail sales via the pharmacy department, while Walmart Pharmacy is an estimated 5% of sales. The expected increased capture rate of prescriptions for the insurance lives will increase prescription volume for these chains and negatively impact the prescription volume for the other chains. Another benefit is that CVS and Walmart employ hundreds of thousands of people who could now have their healthcare insurance directed to their new partner.

Both sets of merger partners point to a new healthcare model that will be created to drive patients into the retailer's locations to receive primary care services. The ability to motivate patients to seek healthcare at retail locations will be an interesting benefit design and marketing challenge. Sharing of data between merger partners could drive programs offering patients healthy choices, incentives for healthy lifestyles, monitoring of unhealthy patterns, and even insurance rates based upon this information. Perhaps loyalty programs could have crossover activities between the retailer and the insurer.

Finally, in both situations, there is an existing long-term business relationship between CVS and Aetna and between Walmart and Humana. What is the risk to CVS and Walmart in these situations? Losing a big client! These mergers ensure that CVS will not lose Aetna for its PBM services, and that Walmart and Humana will continue their strong marketing programs, especially in Medicare Part D.

Retail pharmacies should expect more difficult access to Aetna and Humana patients as preferred networks are created and/or expanded. Reimbursement rates will become

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more aggressive, and performance networks that reward positive health outcomes should become a standard offering. It should be easier for CVS/ Aetna or Walmart/Humana to hit the performance standards, because they will have access to medical, pharmacy, and front-end utilization data.

VERTICAL INTEGRATION: HEALTH INSURER BUYING A PBM

CIGNA/Express Scripts

Watching CVS partner with Aetna and knowing that OptumRx is connected with UnitedHealthcare, it is not surprising that CIGNA targeted Express Scripts (ESI) for acquisition. This will enable CIGNA to provide comparable service offerings and access to data, and level the playing field with its two largest competitors. Once CIGNA can detach from its current PBM, OptumRx (legacy Catamaran), the company will leverage operating efficiencies, data sharing and data mining, and enhance clinical offerings. Again, retail pharmacy should expect more limited networks, perhaps performance networks, all accompanied by more aggressive base reimbursement rates, unless you are a "high performer."

ESI has marketed itself as an "independent" PBM, and that will now change. It will be interesting to see how CIGNA competitors that are using ESI for PBM services will react. Will they keep their business at ESI, or look for alternatives? No doubt CIGNA/ESI will insist there is a fire wall between organizations, but direct competitors may have a different perspective.

The healthcare market will continue to undergo dramatic changes, and pharmacy must adapt to the outcome.

HORIZONTAL INTEGRATION: TWO RETAILERS MERGING

Albertsons/Rite Aid

This coming together of a large supermarket operator with pharmacies and the remaining 2,000 pharmacies of Rite Aid has no vertical integration. Albertsons can use Rite Aid's PBM, EnvisionRx, for claims processing or attempt to sell the business to pay down the large debt of the combined organizations. Usually when an acquisition is announced, the shares of the target company rise with the expectation that the offer will be a premium to the current share price. Unfortunately for Rite Aid shareholders, the opposite has occurred, and the stock price is down almost 30% since the merger was announced. Rite Aid shareholders continue to suffer financially and may not vote to approve the merger.

Reducing administrative overhead by combining headquarters may prove challenging. But the opportunity to cross-sell Rite Aid private-label items in Albertsons stores and Albertsons private label foods in Rite Aid stores should prove profitable. The number of pharmacies will be comparable to Rite Aid before the divestiture of 2,000 pharmacies to Walgreens. The access to additional data will not be as compelling as the health insurer mergers, but can still provide insights into changing consumer dynamics.

IN SUMMARY

The FTC is the wild card in these mergers. Will the FTC agree with the potential synergies that the merger partners have identified, or view them as reducing competition? We are actively watching the Department of Justice in its review of AT&T's planned acquisition of Time Warner for insight into the outcome of the proposed healthcare mergers. If these mergers are all approved, the emergence of a few large players may continue to drive market consolidation as smaller competitors decide if they can compete in this market or must align with one of the big-three health insurers to survive. This is the core question the FTC is wrestling with, and all stakeholders will be lobbying to influence its decision. Either way, the healthcare market will continue to undergo dramatic changes, and pharmacy must adapt to the outcome. What changes are required will be a topic for a future column. **CT**

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