



Walgreens Strikes Drug Distribution and Minority Equity Deal – Transforms Global Drug Market

In a game changing move, three of the major players in the prescription drug marketplace recently announced a partnership to create the largest drug purchaser in the world. The move that could transform the way medications are bought and sold globally.

Walgreens, the largest drug store chain in United States, AmerisourceBergen, the country's second largest drug wholesaler, and Alliance Boots, one of the largest pharmacy chains and drug wholesalers in Europe, announced a 10-year distribution deal that creates a global, vertically-integrated partnership with total revenue of approximately \$180 billion.

There are several market forces driving the deal, including razor-thin margins for drug wholesalers, the explosion of generic drugs due to the expiration of brand drug patents, high margins on generic drugs for PBMs and retail drugstore chains, and slow growth in the absolute number of prescriptions written per year.

Walgreens's main purpose for partnering with the others is to increase its purchasing clout for generic drugs in order to extract price concessions from pharmaceutical manufacturers and lower its cost of goods sold. The company will be able to leverage the size and buying scale of AmerisourceBergen and Alliance Boots to buy generics at cheaper prices. This could give Walgreens a significant advantage over its rivals. Today, generic drugs make up the majority of all prescription drug fills and they are expected to total 90% of all fills within five years.

Additionally, Walgreens officials say the company will benefit from better access to hard-to-find specialty drugs. The majority of drugs in the FDA approval process today are specialty medications. Within 10 years, 50% of the total dollars spent on prescription drugs will be from specialty medications even though the percentage of drug fills will be a small minority.

As part of the deal, Walgreens and Alliance Boots have the option over the next four years to take an equity stake in AmerisourceBergen of up to 23% and to obtain a

total of two board seats. Walgreens already owns a 45% stake in Alliance Boots that it bought last June for \$6.7 billion.

Conclusion

AmerisourceBergen and Alliance Boots are taking a risk with this new alliance because both are large suppliers to thousands of independent pharmacies in the U.S. and Europe, respectively. The companies are betting that having Walgreens as a minority owner will not alienate the profitable base of independent pharmacies, which compete with and have higher cost of goods sold than Walgreens and other national chains.

On its face, it sounds like Walgreens benefits most from this deal. It increased its global stature, influence, and drug buying leverage. The company also lowered its cost of goods sold which should translate to higher profitability. AmerisourceBergen also gave Walgreens a “free” option on its stock with no premium over the current stock price.