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CVS Caremark to Buy Medicare Business for \$1.25 Billion

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CVS Caremark on Friday agreed to buy a Medicare business for \$1.25 billion, an acquisition that may open the nation's largest pharmacy health care provider to further criticism about anticompetitive practices.

Under the terms of the deal, CVS will buy Universal American's Medicare Part D unit, which focuses on the federal prescription benefit program. The purchase will more than double CVS's presence in the fast-growing market, to 3.1 million members from 1.2 million.

CVS has struggled somewhat over the past year, in part due to its shrinking base of Medicare Part D members. In the third quarter, revenues fell 3.1 percent to \$23.9 billion. Profits dropped 19.8 percent to \$820 million over the same period. The stock is off more than 6 percent from its 52-week high.

Shares of CVS on Friday dropped slightly to close at \$34.77, while Universal American's stock spiked nearly 40 percent to \$20.45.

Strategically the deal makes sense for CVS. If approved, it will make the company one of the largest providers of prescription drug services for Medicare recipients. Medicare Part D — which was started in 2006 to address concerns that many seniors lacked drug coverage — today serves nearly 28 million people, according to data from the Centers for Medicare and Medicaid, part of the Department of Health and Human Services.

“Today's transaction furthers CVS Caremark's position as a significant player in one of

the nation's fastest growing segments of the pharmacy benefit management industry," said Per Lofberg, President of Caremark Pharmacy Services, in a statement. "A growing portion of the country's population will receive their prescription drug coverage under Medicare plans, driven both by age demographics and the anticipated shift of retirees from employer based coverage to Medicare that will likely result from health care reform."

The acquisition also provides a potential pipeline of customers for the company's retail pharmacy chain, which operates 7,100 stores around the country.

"It's a natural fit for them," said Kemp Dolliver, an analyst at investment bank Avondale Partners. This is "a population that consumes 40 to 50 prescriptions per year on average and places a relatively high value on face-to-face interaction with a pharmacist."

Such scale helps the company negotiate with drug manufacturers on price, say analysts. Prescription benefit managers handle drug coverage programs for employers and health plans, processing claims on behalf of clients.

Size is also critical when dealing with the government. At the urging of the Medicare agency, many private insurers are consolidating offerings and eliminating policies. That could end up favoring larger players in the market, such as CVS.

"If you're going to be in this business, you want to be big because the government is going to make it so it's all about volume," said Dave Shove, senior analyst at investment bank BMO Capital Markets. "In a more highly regulated environment, scale becomes more important."

But the expansion comes as the federal and state governments are taking a closer look at CVS.

The Federal Trade Commission is investigating whether the company engaged in anticompetitive practices. Attorneys general in 24 states are conducting a similar inquiry, according to CVS Caremark.

Rivals accuse the company of using Caremark, which manages prescription drug plans

for millions of employees across the country, of steering business to its retail CVS pharmacies by charging higher co-pays at competing pharmacies and other unfair practices.

One of the biggest critics, the National Community Pharmacists Association, said on Friday that it was reviewing the details of CVS's proposed purchase.

“It takes a pretty significant degree a chutzpah to expand your role in the market when there is already a serious government inquiry into whether you're involved in anticompetitive and deceptive practices,” said David Balto, a senior fellow at the Center for American Progress, a liberal research organization.

CVS, for its part, said it did not anticipate any challenges in combining the two companies.

“We do not believe this transaction should raise antitrust concerns,” the company said. “The business combination should be positive for customers because CVS Caremark will be more efficient.”