

The Strategic Importance of Wholesaling to Walgreens Boots Alliance

Walgreens Boots Alliance's (WBA) Executive Vice Chairman and Acting Chief Executive Officer, Stefano Pessina, emphasized the strategic and tactical advantages derived from the company's Pharmaceutical Wholesale division. "Our wholesale business is not only highly cash generative while providing a common platform and true international presence, but it is also an enabling business in a sector with scope for further consolidation," he said. "Wholesale lets us enter new markets at scale more rapidly than retail, while its cash flows help give us financial scale and efficiencies. And it brings the mindset of running a low margin operation – with all the rigor and discipline that demands – throughout the combined company's culture. Finally, it is our wholesale relationships and experience that form the basis of the procurement work being done at WBAD [Walgreens Boots Alliance Development GmbH]. Without wholesale, we would not be able to achieve anything like what we are in terms of world class procurement in pharmaceuticals."

WBA's annual report asserts, "Alliance Boots pharmaceutical wholesaling and distribution businesses seek to provide high core service levels to pharmacists in terms of frequency of delivery, product availability, delivery accuracy, timeliness and reliability at competitive prices. Alliance Boots also offers its customers added-value services that help pharmacists develop their own businesses. This includes membership in Alphega Pharmacy, Alliance Boots' pan-European network for independent pharmacies. Alphega Pharmacy had a membership of more than 4,800 pharmacies in seven countries as of March 31, 2014. This is expected to increase following the March 2014 vote by the vivesco pharmacy network in Germany, which has approximately 950 members, to rebrand as Alphega. In addition to the wholesale of medicines and other healthcare products, Alliance Boots provides services to pharmaceutical manufacturers who are increasingly seeking to gain greater control over their product distribution, while at the same time outsourcing non-core activities. These services include pre-wholesale and contract logistics, direct deliveries to pharmacies, and specialized medicine delivery including related home healthcare."

With respect to WBA's relationship with AmerisourceBergen (ABC) and Alliance Boots the Annual Report continues, "From time to time, we make investments in companies over which we do not have sole control, including our investment in Alliance Boots and our investment in AmerisourceBergen. Some of these companies may operate in sectors that differ from our current operations and have different risks.... For example, we [WBA] own only 45% of the outstanding Alliance Boots equity interests as of the date of this report. While we have the right to appoint four designees to serve on the Alliance Boots Board of Directors and veto rights over certain significant Alliance Boots actions under the terms of our shareholders agreement with them, we do not have the ability to control day-to-day operations of that company. Similarly, while we

continued on page 2

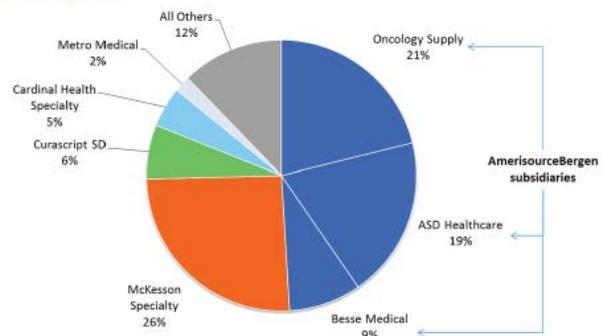
In Brief . . .

- ◆ **AmerisourceBergen Corporation (ABC)** reported a 14.8% increase in revenue (to US\$32.7 billion) and gross profit of US\$1 billion (+25.3%) for its fiscal 2nd quarter ended March 31st. The revenue figure reflects a 13% increase in **AmerisourceBergen Drug Corporation (ABDC)** revenue, and a 25% increase in **AmerisourceBergen Specialty Group (ABSG)** revenue for the period.

- ◆ **Teva Pharmaceutical Industries** recently offered to acquire all outstanding shares of **Mylan** in a cash and stock transaction valued at approximately US\$40 billion, but an increased offer may be forthcoming. Mylan has made multiple offers to acquire rival **Perrigo** which were ultimately declined but continues to be less than enthusiastic about Teva's takeover bid.

- ◆ **Cardinal Health** reportedly acquired **Metro Medical**, the largest independent US specialty distributor (based in Nashville), for an undisclosed sum. *Adam Fein*, president of Pembroke Consulting and CEO Drug Channels Institute, commented, "It's a great move for Cardinal, which dramatically expands its small specialty distribution business while gaining access to new practice settings," and "The Metro deal also puts Cardinal a little closer to the specialty businesses of AmerisourceBergen and McKesson." (see Figure 1). Separately, Cardinal reported an 18% increase in revenue (to US\$25.4 billion) and operating earnings of US\$591 million (+16%) for its fiscal 3rd quarter ended March 31st.

Specialty Product Distribution Revenues to Physician Offices/Clinics, by Company, 2013



Source: Pembroke Consulting estimates. Includes product distribution revenues only. This chart appears as Exhibit 5 in the 2014-15 Economic Report on Pharmaceutical Wholesalers and Specialty Distributors, September 2014. Available at http://drugchannelsinstitute.com/products/industry_report/wholesale/

Figure 1

- ◆ **IMS Health** is preparing to launch a consumer version of its professionally-geared *AppScript* app in May. Currently, AppScript enables doctors to rate and "prescribe" mobile apps for their patients and research suggests about half of the patients who get prescribed apps through AppScript will use them beyond the first month. Moving forward, AppScript will be available to consumers who can use it to download appropriate health apps to help them manage their conditions.

- ◆ **Walgreens Boots Alliance**, in partnership with NBC, is bringing a 25-year United Kingdom tradition to the US this

continued on page 2

Walgreens(cont.) . . .

and Alliance Boots have the right, but not the obligation, to invest in AmerisourceBergen common stock and to designate up to two members of the AmerisourceBergen board of directors in certain circumstances if we achieve specified ownership milestones, we do not and will not have the ability to control day-to-day operations of that company. . . .”

“On March 19, 2013, the Company, Alliance Boots and AmerisourceBergen announced various agreements and arrangements, including a ten-year pharmaceutical distribution agreement between Walgreens and AmerisourceBergen pursuant to which we will source branded and generic pharmaceutical products from AmerisourceBergen; an agreement which provides AmerisourceBergen the ability to access generics and related pharmaceutical products through Walgreens Boots Alliance Development GmbH, a global sourcing joint venture between Walgreens and Alliance Boots; and agreements and arrangements pursuant to which we and Alliance Boots together have the right, but not the obligation, to purchase a minority equity position in AmerisourceBergen and gain associated representation on AmerisourceBergen’s board of directors in certain circumstances. AmerisourceBergen began to distribute all branded pharmaceutical products that we historically sourced from distributors and suppliers, effective September 1, 2013. In the second quarter of fiscal 2014, AmerisourceBergen began distributing generic pharmaceutical products that we previously self-distributed. The levels of generic pharmaceuticals distributed have increased throughout the fiscal year and AmerisourceBergen distributed substantially all of these pharmaceuticals for the Company as of August 31, 2014.”

The Advent of Nanomedicines

(Source: an article prepared by Katrina Megget and published by *PharmaTimes*)

Medicine is going small – nano-small in fact. This is medicine practiced on the scale of less than 100 nanometers, tiny when compared with the diameter of a human hair, which is 80,000 nanometers. But while nanomedicine is on the small side, it promises to be big business, according to the article.

Nanomedicine is the application of nanotechnology to healthcare, and encompasses a number of specialties from technology and engineering to biology and mathematics. Such medicines have already been used to alter the behavior of drug substances – including absorption, metabolism and reducing side effects – but new developments are accelerating, and estimates suggest the market could grow to US\$130.9 billion by next year, says Andrew Owen, chair of the British Society for Nanomedicine.

Targeted nanomedicines are one of the recent breakthroughs – there are clinical trials underway that specifically target cancer cells and HIV, leaving healthy cells intact, Owen notes. The benefits are clear. “Nanomedicine leads to a fundamental shift in how we develop drugs by engineering the bio-distribution into the nanoparticle while letting the chemists focus on biological activity,” says Andrew Hirsch, president and chief executive of the nanomedicine platform company, BIND Therapeutics.

But more than that, nanomedicine also promises early diagnosis and will even lead to disease prevention, says Inês

Mendes Pinto, health unit coordinator at the International Iberian Nanotechnology Laboratory. “Diagnostic nanomedicine will allow us to unravel the mechanism of cell transformation, for example in cancer, and thus enable us to detect early, or even prevent, cell transformation into a malignant state.” These insights are also likely to lead to improved medical devices and treatments tailored to each person’s profile, which will ultimately reduce healthcare costs.

So far, Amgen, AstraZeneca, Merck, Pfizer and Roche have all forged partnerships with BIND Therapeutics, which has developed Accurins, targeted nanoparticles that can use payloads such as small molecules, peptides, proteins and nucleic acids. The future is bright for these innovative therapeutics, and Hirsch, for one, believes nanomedicines will become the new best-in-class. While most research has been directed towards cancer, Matthew Tirrell, Pritzker director and professor at the University of Chicago’s Institute for Molecular Engineering, says this will soon be matched by studies into atherosclerosis, neurodegenerative diseases, autoimmunity and synthetic vaccines against pathogens. Nanomedicine also promises to open the way to personalized medicine, says Mendes Pinto, and it will ultimately converge with other technologies such as miniaturized wireless communication, which will lead to more opportunities like disease-specific and continuous monitoring. “Nanotechnology is set to change the way doctors practice medicine”.

In Brief (cont.) . . .

May with *Red Nose Day*, a charitable event that raises funds and awareness for children in poverty through comedy. In preparation, Walgreens began exclusively selling red noses on Friday, April 17, in support of Red Nose Day which will occur on May 21.

- ◆ **Walmart Stores** unveiled plans to countermand slowed growth in China with 115 new stores in the country by 2017 in cities such as Shanghai, Shenzhen and Wuhan. The company will also invest US\$60 million to remodel more than 50 stores this year. CEO *Doug McMillon* stated, “China is a key strategic market for Walmart. Over the next three years we will increase investment across our diverse business operations in China.”

- ◆ **The Pharmaceutical Research and Manufacturers of America** (PhRMA) elected **Merck’s** chief *Kenneth Frazier* as chairman of the US industry group. PhRMA also announced that *John Castellani* plans to step down as its CEO at the end of the year so a search for a successor has commenced.

- ◆ **Pfizer** pulled its vaccines sales business out of China this month over non-renewal of the import license for its pneumococcal preventative *Prevenar* by the Chinese government. The reasons behind the license not being renewed were not disclosed, but Pfizer indicated that it would result in a shortage of the vaccine in the country. The company intends to introduce the next-generation version of the vaccine, *Prevenar 13*, in China at some point in the future.

(Sources: AmerisourceBergen, Cardinal Health, Drug Store News, *PharmaTimes* and *Scrip*)