Quiz #7: Monday, May 13, 1996

(10 points) The story below from the Wall Street Journal of April 25, 1996 describes the cancellation of the $1.8 billion tender offer by Rite Aid for Revco following Federal Trade Commission opposition to the transaction on anti-competitive grounds. Read the following excerpts from the article and answer the questions at the end.

HD Rite Aid Corp. Abandons Revco Deal, Blaming FTC for Aggressive Opposition ---
U.S. Agency Calls Collapse Of $1.8 Billion Accord a Victory for Consumers
BY Matt Murray and Bryan Gruley, Staff Reporters of The Wall Street Journal
PD 04/25/96
SN The Wall Street Journal, PG A3
CY (Copyright (c) 1996, Dow Jones & Company, Inc.)
LP Rite Aid Corp. abandoned its $1.8 billion tender offer for Revco D.S. Inc. and blasted the Federal Trade Commission for its aggressive opposition that killed the drugstore deal. . . .
TD The FTC, which had argued the combined drugstore companies would have the clout to raise prices too much in some markets, called the collapse of the deal "a victory for consumers." George Cary, deputy director of the FTC's Bureau of Competition, rejected Rite Aid's charge that the agency acted arbitrarily, pointing out that the agency has cleared five drugstore acquisitions in the past two years, including two by Rite Aid and one by Revco.

The collapse of the deal is a stunning setback for Rite Aid and, some believe, for the chain-drugstore business as a whole. Some rivals feared the acquisition would have created a drugstore colossus -- with close to $11 billion in annual sales and more than 4,500 stores -- twice the number of nearest rival Walgreen Co. But industry executives and analysts said the FTC's actions could threaten growth prospects for big chains by putting a damper on acquisitions, which drugstores see as a way to slash costs.

Some executives in the $87 billion industry also say bigger chains are crucial in fending off pressure from managed-care groups, which are squeezing profits for the drugstores by cutting the fees they pay pharmacies to dispense drugs to consumers. . . .

Mr. Cary also said that a combination of Rite Aid and Revco, which have the two largest store counts of any drugstore chain, would be a unique circumstance. . . .

The head of a drugstore trade group agreed. "We do not believe the FTC is sending any signal indicating absolute opposition to consolidation in this industry," said Ronald L. Ziegler, head of the National Association of Chain Drug Stores. . . .

In composite trading on the New York Stock Exchange, Rite Aid shares fell $1.75 to $29.875. Revco shares fell $1.875 to $24.125. . . .

Rite Aid said it didn't have to pay a breakup fee, but that it would take a fiscal first-quarter charge of $15 million to $16 million, or 10 cents to 12 cents a share, for costs related to the aborted deal. Mr. Grass ruled out a future Revco bid. . . .
Trouble From the Outset

Chronology of tensions between the drugstore companies and the FTC

Nov. 30: Rite Aid agrees to buy Revco for $1.8 billion, creating a giant chain with more than 4,500 drugstores and sales of about $11 billion.

Dec. 28: FTC requests more information related to proposed deal. Deadline for tender offer is extended, in what will be the first of a constant stream of extensions.

Feb. 8: FTC says Rite Aid and Revco both violated consent decrees requiring them to sell certain stores, and appoints trustees of its own to sell the branches in question. While the consent decrees stem from prior acquisitions, the squabble hints at strained relations between the agency and the firms.

Feb. 20: Merck & Co. files an antitrust lawsuit against Rite Aid and other retail pharmacies, alleging they joined in a conspiracy to boycott a contract for Merck's Medco unit to administer the prescription-drug benefit program for employees in the state of Maryland. Merck lost the contract last winter after more than half the state's pharmacies refused to fill prescriptions. Rite Aid denies the accusation.

April 17: FTC panel votes to block Rite Aid–Revco deal, citing concerns about higher prices.

April 22: Rite Aid offers to shed about 340 stores -- about 8% of combined entity's stores -- in hopes of heading off FTC's threat to sue to block the deal.

April 23: FTC rejects the settlement proposal and restates intention to block the deal.

April 24: Rite Aid drops its tender offer for Revco.

Why do you think that the stock prices of both Revco and Rite Aid fell when this story was announced? Link your explanation to the evidence you have learned in the course.
How do you think the stock price of Rite Aid and Revco competitors (e.g., Walgreen) reacted to this announcement?  *Why?*

How do you think the stock price of Rite Aid and Revco suppliers (e.g., Merck) reacted to this announcement?  *Why?*
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