BN WellPoint Agrees to Buy WellChoice for $6.5 Billion (Update4)
Sep 27 2005 16:49

(Adds investor's comment in fourth paragraph.)

By Geraldine Ryerson-Cruz and Kristen Hallam

Sept. 27 (Bloomberg) -- WellPoint Inc., the largest U.S. health-insurance provider, agreed to buy WellChoice Inc. for about $6.5 billion to expand into New York.

WellPoint will pay $77.23 a share in cash and stock for WellChoice, New York's biggest medical insurer, the companies said today in a statement. That's 9.4 percent more than New York-based WellChoice's closing price of $70.60 yesterday.

WellChoice will bring WellPoint 5 million customers in New York and increase the number of Americans covered by the Indianapolis-based company to 33 million. The purchase will expand WellPoint's lead over No. 2 UnitedHealth Group Inc. in an industry that accounts for $657 billion in annual premiums, or 5.3 percent of the U.S. economy.

``This is clearly a move to increase scale in an industry that's consolidating,'' said Christopher Bonavico, a San Francisco-based fund manager for Delaware Investments, which owned $2.6 million shares of WellPoint as of June 30 and also owns UnitedHealth stock. He spoke in a telephone interview today. ``They clearly believe that scale matters in terms of having more of an offering of national accounts and more power locally'' to negotiate costs with health-care providers, he said.

WellChoice holders will receive $38.25 in cash and 0.5191 share of WellPoint for each WellChoice share, the companies said in today's statement. The transaction, subject to shareholder and regulatory approvals, probably will be completed in the first quarter of 2006, according to the statement.

WellPoint's investment bank advisers were Goldman Sachs and Banc of America. WellChoice was advised by Lazard Ltd.

Shares of WellChoice jumped $4.91, or 7 percent, to close at $75.51 at 4:18 p.m. in New York Stock Exchange composite trading. The stock had almost doubled in the 12 months before today and tripled since November 2002. WellPoint declined 8 cents to $75.01, for a 75 percent gain in the past 12 months.

Consolidation

The transaction shows how the medical-insurance industry is consolidating in the same way that the Baby Bell telephone companies have done, leaving a handful of giants. WellPoint itself was formed last year when Anthem Inc. bought WellPoint Health Networks Inc. for $20.8 billion and took its name.

UnitedHealth, based in Minnetonka, Minnesota, last year bought Trumbull, Connecticut-based Oxford Health Plans, with 1.5

million customers in the New York area, for $4.6 billion. The proposed $8.14 billion UnitedHealth purchase of PacifiCare Health Systems Inc., based in Cypress, California, will increase its customer total to 25 million from 22 million.

New York Market

``The New York area is a very good market for insurers, with a lot of large companies headquartered there that can use their national coverage,'' said Michael Obuchowski, who helps manage $35 million at New York-based Altanes Investments LLC, including health insurance shares, in a telephone interview today.

Cigna Corp. said Aug. 3 that it had 9 million members at the end of the second quarter. Aetna Inc. said July 28 that it had 14.4 million members as of June 30.

``WellPoint wants to be national, and New York was obviously a place they needed to be,'' said Les Funtleyder, a health-care strategist at Miller Tabak & Co. in New York, in an interview today.

Spitzer

New York Attorney General Eliot Spitzer, who has won antitrust concessions from companies including Federated Department Stores Inc., may be among state politicians who decide to oppose the merger, said Scott Fidel, an analyst at J.P. Morgan Securities Inc. in New York, today in a note to clients. Spitzer declined to comment on the merger through a spokesman.

``We expect the merger could take some time to be completed as WellPoint will need to negotiate with a number of regulatory and consumer groups in the state, particularly given that WellChoice is the largest health insurer in the state,'' Fidel wrote in the note.

WellPoint is the largest operator of Blue Cross and Blue Shield health programs, covering one in every three U.S. customers of the plans. The addition of WellChoice, the biggest operator of such plans in New York, will add a 14th state. The company has non-Blue Cross operations in other states.

The New York Public Asset Fund, created in 2002 to hold WellChoice shares when Empire HealthChoice Inc. was converted to a for-profit company, agreed to back the transaction, the companies said. The fund owns 52 million WellChoice shares, or 62 percent of those outstanding, and would receive $1.99 billion in cash and 27 million shares of WellPoint, based on yesterday's closing price, the companies said.

Purchase Price

``The purchase price represents a nearly 50 percent premium above the company's stock price from the beginning of this year and, more importantly, a more than threefold increase above the stock's $25 per share initial public offering value in 2002,'' said Mallory Factor, chairman of the New York Public Asset Fund's board, in an e-mailed statement today.

The Fund's primary financial adviser was Sagent Advisors, and the secondary adviser was Blackstone Group LP.

WellPoint Chief Executive Officer Larry Glasscock, 57, and UnitedHealth CEO William McGuire have been expanding to cut costs through economies of scale. After the second quarter, WellPoint said it may reduce costs by $150 million this year compared with the two predecessor companies last year.

Employers' costs for health insurance have jumped 73 percent since 2000, according to a survey released this month by the Kaiser Family Foundation, which studies health policy, and the Chicago-based Health Research and Educational Trust, an arm of the American Hospital Association. Research by benefits consultant Hewitt Associates indicates costs will rise 12.6 percent next year.

Costs, Premiums

``When I look at our combined companies, I think we'll be even better able to reduce costs and help pull down the rising costs of health insurance,'' WellPoint's Glasscock said today in a call with reporters. ``This merger will not in any way add to premium increases.''

The merger may help WellPoint negotiate bigger discounts from hospitals and doctors, which would result in smaller medical cost increases, Funtleyder said.

``Getting larger really does matter,'' Funtleyder said. ``Scale helps because it helps drive greater discounts. The more enrollees you have, the better off you are in terms of costs.''

Selling and general expenses for WellPoint fell $25 million in the first quarter and $35 million in the second. The company said in July that, by next year, savings will total $250 million as WellPoint merges sales forces and eliminates administrative costs.

Moody's Investors Service affirmed its ratings on WellPoint's debt, including senior unsecured notes at Baa1, and maintained a stable outlook. Long-term debt will be used to finance $2.7 billion of the cash portion of the acquisition, Moody's said.

(To hear a replay of WellPoint's conference call with investors and analysts, see {WLP US <Equity> CNAV <GO>}.

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Story illustration: For information on WellPoint's acquisitions, see {WLP US <Equity> CACS 21 <GO>}. For WellChoice's share-price history, see {WC US <Equity> GP D <GO>}.

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