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Billionaire Stefano Pessina cannily took control of Walgreens using the chain's own money. Now he's squaring off with CVS Health for drugstore domination. Can a brilliant dealmaker become a killer retailer?

by
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Photograph by **THE VOORHES**

On Jan. 9, 2015, the executives of the newly consecrated Walgreens Boots Alliance came together to ring the opening bell at the Nasdaq stock exchange. Standing in the center was CEO Greg Wasson, a onetime pharmacy intern from Indiana who had worked his way to the top of Walgreens, the 8,000-plus-location American drugstore chain with $76 billion in sales. Wasson had spearheaded the company's biggest ever acquisition. Next to him, grinning widely, was the man who had assembled the acquired company: Stefano Pessina, an Italian billionaire who had started with one local pharmaceutical distributor in 1977 and, through shrewd and voluminous dealmaking, built it into the $40 billion, 4,600-store Alliance Boots.

As the bell clanged and the ticker tape fluttered from the ceiling, the two embraced, now officially partners in one of the drug industry's biggest and boldest mashups ever. But for all the onstage camaraderie, there was only one person in charge. Just a month earlier, Wasson, who was slated to become CEO of the mammoth merged enterprise, had suddenly announced that, at age 56, he would retire upon the deal's consummation.

It was a surprise. Less surprising for many was the person named interim and later permanent CEO: Pessina. It appeared that the snake had somehow swallowed the elephant—or, in the words of many former Walgreens executives, the iconic American brand had been bought with its own money.

"I AM NOT A RETAILER," PESSINA, THE CEO OF WALGREENS, READILY ADMITS. "I AM NOT A WHOLESALER ANYMORE. I AM A TEAM BUILDER AND A COMPANY BUILDER."

Today the 74-year-old Pessina, who owns some 13% of WBA, is firmly in control. And he's not done swallowing companies. Before Walgreens had come close to digesting Alliance Boots, Pessina had announced plans in October to buy Rite Aid, the No. 3 player in the U.S., for $17.2 billion. He says there are more deals to come. "I am really convinced," he said on a recent earnings call, "that vertical integration is a necessity for this market to control the costs in the health care arena. We are always open, even to partnerships."

Onlookers were taken aback by Pessina's audacity—*Who is this guy?* But this is merely the latest maneuver in a career filled with ever more ambitious transactions. The story of how a septuagenarian Italian became a key player in how U.S. consumers buy deodorant and Lipitor is a saga for the ages. It's replete with everything from high-stakes negotiations and romance to bitter accusations of backstabbing and betrayal. It's a heck of a tale, and one whose ending has yet to be revealed.

Pessina's track record is impeccable. He has constructed a giant corporate edifice in the service of creating a truly global health care enterprise. His pharmaceutical wholesaling business and his drug stores each now operate on four continents. Still, Pessina's last few moves transformed his firm from primarily a wholesaler to a company heavily dependent on U.S. retail stores, a graveyard for more than one swaggering foreign adventurer. (Remember Tesco? Marks & Spencer buying Brooks Brothers? Sainsbury's? I thought not.)

In the U.S., his retail strategy is to infuse the panache of Boots into the efficiency and convenience of Walgreens stores. As WBA bulks up, it is girding itself to take on giant CVS Health in the battle for control of consumers' medicine chests. Can Pessina give its biggest U.S. rival a run for its money—or has the master acquirer finally done one deal too many?

One bottle of San Pellegrino water. It's the closest thing to a personal item visible in Pessina's office in Walgreens Boots Alliance's headquarters in Deerfield, Ill., near Chicago. It's the only evidence that a human being at least occasionally works there. There are no photographs with luminaries, no mementos of product launches or even stacks of files. Perhaps that's because Pessina actually lives in Monaco and spends so much time on the road. It may also be because he isn't interested in typical CEO activities. He doesn't visit many stores or pose for selfies with the employee of the month. He doesn't obsess over a particular SKU. "I am not a retailer," he readily admits. "I am not a wholesaler anymore. I am a team builder and a company builder."

Pessina had never planned to be a businessman. He attended the prestigious Politecnico di Milano, intending to become a nuclear engineer or an academic. But during the turbulent late 1960s, he was repelled by his fellows students' push for what he viewed as lax grading standards. "I was disgusted," he says. He quit school and landed a job heading the statistical department of A.C. Nielsen's Italy office. When Nielsen asked him to move to Chicago, he declined. "I had learned what I could learn," he says.

Instead, he turned his attention to a project for

PHOTOGRAPHS BY TAYLOR CASTLE

LIFETIME DEAL? PESSINA, LEFT, MET HIS "LIFE PARTNER" AND FELLOW EXECUTIVE ORNELLA BARRA WHEN HE ACQUIRED HER COMPANY DECADES AGO.

his father, Oreste, who owned a small, struggling pharmaceutical wholesaler in Naples. Oreste hoped his son's facility with numbers would help him. Pessina says he turned the business around—then began helping his father's colleagues do the same in return for a small stake in their companies. He soon realized the sector was ripe for consolidation.

Pessina became enamored with transactions—so much so that in 1984 he fell for Ornella Barra, the glamorous owner of a small Ligurian drug wholesaler, whose company he later bought. The two never wed (Pessina remains married to his first wife, from whom he separated decades ago), but they are "life partners." Barra has worked with Pessina ever since, holding senior executive positions in every iteration of his company. Today she heads Walgreens' global wholesale and international retail divisions. Says Barra: "The secret of our life and working together is that he's the boss. We have different opinions, but when he takes a decision, it's also my decision."

After Italy, Pessina set his sights on France, where, with Barra at his side, he rolled up 30% of the drug-wholesaling market within five years and then moved into other countries. He became a master at understanding the quirks of each region, in part by partnering with—and then outmaneuvering—smaller players. His method: Buy a stake in a company, help improve the bottom line, and then gain enough control to merge with or buy yet another one. It always seemed he was buying a new company before he had even finished unwrapping the last one.

"It's a game at the end of the day," says Pessina, who estimates he has made 1,500 acquisitions. Adds Ken Murphy, a deputy for 17 years and the head of WBA's global brands: "He's got an objectivity which is quite stunning. He never gets emotionally embroiled; he never loses himself. He never becomes a slave to the deal."

For all of Pessina's seeming addiction to transactions, there was a broader strategy at work: He was convinced that the drug-distribution business was destined to consolidate. And so Pessina kept rolling up ever bigger targets. Alliance Santé, as his company was called by the mid-1990s, expanded further into Europe until 1997, when Pessina, believing he could rationalize the costs of pharmacies with his wholesale business, merged with UniChem, one of Britain's largest pharmacy chains and a public company. The move added retail expertise and the experience of a public listing to his portfolio and made him wildly wealthy. Yet he struggled to integrate the two cultures—and, in a precursor of things to come, took over as CEO. (He relinquished the position in 2004.)

Next, Pessina boldly set his sights on Boots, the largest and best-loved English drugstore chain. He spent several frustrating years trying to persuade three different chief executives to sell. In 2005 he finally got CEO Richard Baker to take the bait. The companies combined to form the new Alliance Boots.

Although the European press often calls him "silver fox" for his spiky white hair and blue eyes, Pessina lacks charisma on first impression—until you ask him about a deal or the future of the industry. Then his eyes crackle with energy and he displays a penetrating clarity (not to mention a refreshing absence of CEO pablum).

Pessina has maintained his focus, plowing his equity into the next deal. That's one reason his fortune is currently estimated at more than $12 billion. He insists he's not motivated by riches. "When you have some money," he says, "if you have 10 times more, it's absolutely irrelevant." Pessina wants to keep building.

Soon after the merger with UniChem, Pessina joined forces with private equity giant KKR. He and its health care chief, Dominic Murphy, decided to take Boots private, ultimately beating back

WALGREENS, THEN AND NOW: LEFT, A WALGREENS PHARMACY IN 1964; RIGHT, A CONTEMPORARY VIEW. PHARMACIES ACCOUNT FOR TWO-THIRDS OF WALGREENS BOOTS ALLIANCE'S U.S. SALES.

LEFT: COURTESY OF WALGREENS; RIGHT: LUKE SHARRETT—BLOOMBERG VIA GETTY IMAGES

several rivals to complete a $22.3 billion deal—Europe's largest leveraged buyout ever, with a stunning $11.8 billion in debt. The transaction, closed in the summer of 2007, catapulted Pessina into the spotlight—CEO Baker abruptly resigned, leaving Pessina in charge again—and spurred fears that a revered brand would be ruined by the foreign financiers.

But he flummoxed the skeptics. Boots didn't fail. Pessina and KKR cut jobs and costs but also invested, sprucing up the stores and differentiating them with an increased emphasis on beauty and other higher-margin products. Alliance's distribution unit signed a radical agreement with Pfizer to become the exclusive wholesaler of its drugs in the U.K. The deal provoked howls of outrage until it was shown to have substantially reduced the prices consumers paid.

Pessina's ambitions and confidence only continued to grow. His goal remained consistent: to create a global health care company. And Alliance Boots couldn't be truly global without the U.S.

Back in the heartland, Walgreens CEO Wasson was facing tough choices. He had taken the top post in 2009 with a mandate for change. But the chain had reached the limits of organic growth. The financial crisis was crimping consumer spending. Walgreens' homespun way of doing things seemed dated in the age of the Internet.

It had worked for so long. Charles Walgreen and his descendants had built a behemoth by innovating and offering a great customer experience. Walgreens chose the best locations and hired the best pharmacists and shopworkers, paying them more and promoting from within. It delighted customers early on, giving away free goldfish with a $1 purchase and inventing the malted milk shake in 1922.

And then—from approximately 1975 well into the 1990s—the company went turbo, blowing past rivals to become one of the largest retailers and one of the best-performing stocks in America. It was lauded in the book *Good to Great* for its performance—trouncing the stock market by a factor of seven—as well as its ethical, modest, people-focused approach. "I always considered it a paternalistic-type company," says Jeff Rein, Walgreens' CEO in the mid-2000s.

Rein's successor, Wasson, put the brakes on rapid store expansion but did undertake a few acquisitions, including the New York–based Duane Reade chain in 2010. He cut costs and brought in some outside talent. He also vowed to use Walgreens' clout to stand up to pharmaceutical benefits managers (PBMs), which represent organizations whose employees purchase a lot of medications. PBMs were lowering reimbursement rates to chains.

Wasson decided to take on Express Scripts, one of the largest PBMs, as his test case. He announced in 2011 that the company would stop doing business with it, believing that customers would be more loyal to their pharmacy than to a PBM.

He was wrong. Customers streamed out the door and Walgreens' earnings plunged. Says Adam Fein of Pembroke Consulting: "They brought a

BOOTS, OLD AND NEW: LEFT, A BOOTS OUTLET IN 1962; BELOW, A MODERN STORE, WITH CUSTOMERS LINING UP TO BUY THE COMPANY'S POPULAR NO7 BEAUTY PRODUCTS.

LEFT: LOCAL WORLD/REX/SHUTTERSTOCK; RIGHT: JAMES VEYSEY—CAMERA PRESS/REDUX

knife to a gunfight. It was a massive miscalculation, and millions and millions of scripts walked out the door and never entered a Walgreens again."

Wasson had previously discussed a possible Boots deal with Pessina. But suddenly overseas growth had become more of an imperative. Pessina, not surprisingly, was game. As he puts it, "We saw that we were sharing values."

Still, Walgreens was nervous about a full-on merger, so Pessina proposed a complex two-step process in which Walgreens would acquire 45% of Alliance Boots in 2012. Three years later, if both parties were satisfied, it would buy the rest.

In July 2012—weeks after the first step of the deal was announced but before it had closed—Walgreens capitulated and began working with Express Scripts again. The truce pleased investors, who boosted Walgreens' stock 12%. The biggest beneficiaries: Pessina and KKR, who had agreed to receive a set number of shares (rather than a set dollar amount) from Walgreens.

Pessina out-negotiated his counterparts, say sources on both sides. Says Barclays analyst Meredith Adler: "I thought it was pretty irresponsible to negotiate when the thing was still going on. They [Walgreens] gave away a lot of stock value. I used to joke that KKR or Pessina had negotiated both sides of the transaction." (A WBA spokesperson says the fixed number of shares "helped align both parties' interests to maximize synergies.") Observes Murphy: "It was men against boys."

The two companies—now engaged, with marriage looming—began to explore the practicalities of getting hitched. Teams flew back and forth between Nottingham, England—Boots' home—and Deerfield to uncover best practices. More seemed to come from Boots than the other way around. Wasson had long wanted to improve the retail part of Walgreens stores (two-thirds of sales came from the pharmacy), and he saw Boots, which did more than half its business in retail, as the ideal laboratory. To that end, Alex Gourlay, a Boots lifer, was installed to help run Walgreens USA.

Then a massive error tilted the balance of power even further in Boots' direction. Walgreens had forecast that the prices of generic drugs would fall—only to realize that in fact they were rising. In the summer of 2014, the company abruptly slashed its projected 2016 profits by a third. Walgreens shares dropped 14% in a day. Says Adler: "It was a complete shocker."

The aftermath only made Walgreens look worse. Unnamed company executives and directors were quoted in a *Wall Street Journal* article blaming the disaster on CFO Wade Miquelon and a second executive. A Wasson confidant who had been well regarded, Miquelon had just stepped down, in a planned retirement. He was incensed by the impression that he had resigned because of the forecasting miscue.

Miquelon filed a defamation suit against Walgreens. Among his claims: that Pessina and Wasson had been aware that the company was struggling to meet its projected profits and that they had pushed Miquelon to find a way to reach the targets. (The suit is still pending, though seven of nine counts have been dismissed. Miquelon did not respond to requests for an interview.)

OLD REGIME: GREG WASSON, LEFT, STEPPED DOWN AS WALGREENS' CEO. WADE MIQUELON, ITS FORMER CFO, FILED A DEFAMATION SUIT AGAINST THE COMPANY.

Miquelon's complaint included emails in which he was praised by Wasson and told he could be a CEO candidate one day, along with one from Wasson that reads, "Let's push for a 6 somehow," referring, Miquelon asserts, to earnings per share. After Miquelon objected, Wasson texted "No choice. Need a 6. We'll find a way." (Today WBA is projecting $4.30 to $4.55 in earnings per share for 2016.) In a legal filing, Walgreens argued that "there is nothing improper about a CEO asking his CFO if better results are possible, e.g., through greater cost reductions, synergies, or share buybacks." For his part, Pessina claims ignorance. "We were not in charge," he says. "If we had been in charge, this would not have happened, I can assure you."

Walgreens and Boots had decided to proceed with the second step and complete the merger ahead of schedule. But Wasson's credibility took another blow when the board opted against an inversion, in which the company would have moved its headquarters to Switzerland and bolstered after-tax earnings by an estimated $600 million. The timing was lousy, coming just as inversions became a political issue, excoriated by President Obama and many others. Walgreens chairman Jim Skinner, a former CEO of McDonald's, says the two-step deal made the maneuver vulnerable to IRS challenges.

Confidence in Wasson began to wane, but as late as Nov. 24, 2014, Walgreens' proxy stated that he would run the company when the deal was consummated at year's end. Pessina says he wanted Wasson to be CEO of the merged company and was surprised when he decided to step down. "Six months before," Pessina says, "I would have said that Greg would have stayed. And after, things began to be difficult. You have seen, with the team and with him, the shareholders were not happy."

The comment is oddly elliptical and passive given that Pessina is a shareholder controlling 13% of the company's stock, with allies KKR and activist fund JANA Partners holding sway over another 4.7% and 1.1%, respectively. "It was not us [who pressed for Wasson's departure]," Pessina insists. "On the contrary, I tried to help Greg as much as possible."

Wasson recalls it differently. "It was my decision to retire," he says. "I really had spent some time reflecting; I had just put the biggest merger together. Now there would be another three to five years of integrating the merger. I had been CEO for six years and thought, Now's the time."

Some of the shareholders, however, were about to be very happy indeed. When the deal was finalized, KKR cashed out a profit of $5.4 billion while still retaining a substantial stake. Pessina emerged with 141 million shares, which are now worth nearly $11.3 billion.

After a desultory search, Pessina moved from acting to permanent CEO. He says he didn't aspire to the job. "I'm here because I wasn't lucky and I didn't have someone to do this job," he says, sounding a little put out that he has to spend time overlooking a snowy parking lot in Deerfield when he could be doing deals. "You can see where my heart is."

The senior management team is now dominated by former Boots executives. The board, too, has been restructured, with nearly half the members having been appointed by KKR, Pessina, or activist investor JANA Partners, which ended up with two seats and the right to veto a third after buying just 1% of the company. Pessina says WBA will soon have more representation from the Walgreens side. The many departures suggest that not everyone believes him.

Amid all the dealmaking and drama, there is still the crushingly difficult work of integrating two enormous, unwieldy, and proud companies across sprawling geographies. The good news is that in some ways, Boots and Walgreens feel like cousins separated by an ocean. Both are venerable (Boots is 166 years old; Walgreens, 115). Both were named for founders and run by family members for decades. Both had paternalistic cultures. Most of all, both had reputations for quality, service, and trustworthiness.

Yet there are also significant differences—which make some analysts wonder whether this will be the Pessina deal that finally disappoints. For starters, Boots shops feel like upscale emporiums. In Derby, 2½ hours north of London, its store resembles the ground floor of a U.S. department store. Prominent

WASSON: MIKE MCGREGOR—CONTOUR BY GETTY IMAGES; MIQUELON: APRIL L. BROWN—AP space is devoted to high-end beauty brands like Chanel and Clarins and cheaper ones like Max Factor. Advisers roam the aisles to help customers test a new lipstick or toner, especially Boots' popular house brand, No7. In a London outpost, an adviser pulls out a spectrometer to test my skin hue, then recommends complementary makeup colors (including a "warm paprika" lipstick). A Boots store feels like a Sephora with health care attached.

Walgreens stores aren't problems per se—they're clean and bright. The real issue is that generations of Americans have been trained to visit them for "convenience," picking up a quart of milk and some toilet paper, or maybe a prescription, and getting in and out as fast as possible. Efficiency, rather than lingering to try, say, a luxurious beauty item, is paramount.

That seems like an obstacle—but Pessina argues it's an opportunity. He wants to inject a little Boots into Walgreens. That mission falls to Gourlay, a coal miner's son who started working at a Glasgow-area Boots at age 16, and oversaw the chain before being sent to Walgreens in 2013. He has the passion for stores that Pessina lacks; Gourlay has visited some 500 Walgreens. Gesturing toward a color-coded map in his office that plans out the next several years, he argues that the company is poised for success. Trials of No7 in Phoenix have given Walgreens the confidence to roll it out to 2,000 stores later this year, and Gourlay thinks such products are not out of reach for Walgreens customers. "We had to stand up on our own two feet in retail [in the U.K.]," he says, in a Scottish burr that hasn't softened after two years in the Midwest. "We think we can do that in the U.S. We've been testing No7 and Soap & Glory [another brand]. It's not overly posh. It's mid-market. We're offering convenience and the availability of beauty advisers. These are 'masstige' products, but they are characteristic of high quality."

The Boots team is careful to sound humble. "We will never bring Boots here," says Pessina. "We will bring the products, we will bring ideas, but not Boots."

Still, making over Walgreens will be a costly and time-intensive endeavor—one that has been tried unsuccessfully before—in an environment that offers many other options for beauty, from Sephora to Ulta to CVS. There's also the fact that the moderate-price realm of the U.S. retail market is in serious trouble as the middle class continues to shrink. Finally, there is the specter of online retailing. Walgreens has superb retail locations. But how much does that matter when, for the first time, more Americans shopped online on 2015's Black Friday than visited stores? (Indeed, Walgreens has fallen behind its competitors in some of its digital initiatives.)

All this would seem like more than enough to keep Pessina occupied. But in October, he announced that Walgreens Boots Alliance was buying, for $17.2 billion, Rite Aid (or as he pronounces it, with a rolling "r" and a few extra syllables, "Rrrrrrriiiiite Aiiiiide"). The scale advantages are obvious, but the costs of executing another merger and the challenge of folding in yet another culture (and more debt) into this already unwieldy company seem daunting. Moreover, for antitrust reasons, Walgreens may be forced to sell off more stores than the 1,000 it has accounted for.

And WBA will have to keep improving its pharmacies as the category is buffeted by massive change. Both CVS and Walgreens have struggled to contain spiraling drug costs. That's easier for CVS to accomplish, since it owns its own PBM, Caremark.

CVS and Walgreens are pursuing opposite strategies. CVS is emphasizing its pharmacies and health clinics even as Walgreens pushes consumer products. CVS has made health its unifying concept, punctuating the choice by adding "Health" to its name and making the bold decision to stop selling cigarettes. Says the CEO of another competitor, with admiration: "CVS has been really consistent and is building a brand around what it stands for."

Pessina has countered with what he does best: more deals. One, with wholesaler AmerisourceBergen, has already cut drug-acquisition costs. WBA will also buy medications directly (rather than through a wholesaler) from Valeant, the once-hot, now-beleaguered drug manufacturer. If Pessina can get others to agree to such terms, he could save Walgreens billions.

Can WBA thrive? It has $14.2 billion in debt and will carry as much as $31.2 billion—more than three years' worth of Ebitda—if the Rite Aid purchase is approved. That's a load that could constrain WBA's ability to invest. Also, measuring success is tough at the moment. Because the companies merged and reorganized, it's nearly impossible to compare current results with the past. Says Scott Mushkin of Wolfe Research: "They don't provide pro forma numbers. They could be down year over year." WBA shares have performed well, suggesting that investors are giving Pessina the benefit of the doubt for now.

Ultimately, Pessina is focused on vertical integration. "The industry has to change," he says. "In 10 years all of the distribution in the U.S. will have changed. We have to reduce dramatically the cost of distributing drugs and, more generally, products. We cannot sustain the explosion of the cost of health care."

Pessina may well be right, but he can't ignore the heart of retailing: the daily interaction with the customer. Says Bill Rudolphsen, the company's CFO from 2004 to 2008: "I understand it's the right thing to do to go global, but there's all this other stuff. It's so much about the culture." He recalls sitting in the boardroom, with portraits of three generations of Walgreen family members on the wall, and feeling their eyes on him: "When I sat at one end of the table, they were all looking at me. When I sat at the other end, they were all looking at me. It was part of the culture. They were all always watching me."

Pessina, unsurprisingly, feels less burdened by that legacy. "The survivors are the people who are able to change," he says, "and we have always been at the forefront. Not always are we right. But most times we are right, and this is why we are alive." He has won Walgreens. Rite Aid is on his plate. And Pessina will feel even more alive when he finds the next deal after that. F