Walmart and CVS have 15,000 combined stores. Why are both trying to buy health insurance companies?

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The economics of healthcare in America is making for some strange bedfellows. CVS, the behemoth pharmacy chain, plans to buy Aetna, a 22-million member health insurer, for $69 billion. Less than two weeks ago, it became public that Walmart, where one in four Americans shop each week, is considering an acquisition of another insurer, Humana.

Why would these two massive retailers want to buy health insurers? Think millions of customers under one roof buying insurance, visiting health clinics and—importantly—filling prescriptions. These merged insurer-retailers could have lots of price-setting leverage in dealing with pharmaceutical companies and hospitals. But consolidation like this also can threaten competition—and in healthcare markets, that is a demonstrated danger.

To see clearly what's going on here, it helps to distinguish, as regulators do, between horizontal and vertical mergers. When two competitors in the same business consolidate, that's a horizontal merger. Hospitals, for instance, have been merging horizontally for decades. There is some evidence that such mergers can improve quality of care, particularly if two small hospitals join forces and become more efficient. But there's also plenty of data showing that when regional health systems get too big, that can drive up prices. Some believe the reason prices for inpatient hospital care in Southern California are 70 percent lower than in

Northern California is because the hospital market down here is very competitive compared with the highly consolidated picture up north.

Last year the federal government stopped two big attempted horizontal mergers in the health insurance industry: Anthem's proposed takeover of CIGNA and Aetna's proposed merger with Humana. The Department of Justice blocked both citing concerns about reduced competition, increased prices and stifled innovation.

So the insurers are taking a different tack by going vertical. A vertical merger is when companies at different stages of the production process merge.

Regulators from the Justice Department and the Federal Trade Commission will take a close look again. But this time insurers hope to make the case that by integrating with retailers they will be getting bigger in a way that creates more competition, not less. They will stress that for some forms of healthcare, they will be able to compete directly with hospitals and physician groups. With 5,000 Walmart stores and nearly 10,000 CVS stores in the United States, they can also claim an ability to make healthcare more accessible and affordable in many communities.

Two other factors are driving these retailers' interest in healthcare. First, it's where the money is. Americans spent an average of $10,348 per person on health care in 2016, accounting for 17.9 percent of the nation's Gross Domestic Product. For retailers—who routinely operate with low profit margins—the high margins of healthcare must look very attractive.

Second, Amazon—the giant of consumer sales and noted disrupter of traditional business models—announced in January that it was partnering with Berkshire Hathaway and JP Morgan Chase to create a new healthcare company. Its initial goal is to use technology to reduce costs and improve outcomes for the three firms' combined 1 million employees. But no one forgets that Amazon also started out selling just books. This is another motivator for the retailers and insurance companies to merge quickly.

Once merged, these huge retail-health systems could steer policy holders to less expensive services—like clinic visits or pharmacist visits—and possibly drive down drug prices as well. Health outcomes may even improve. But prices could also rise. If a big CVS-Aetna or Walmart-Humana system dominates a region, it could negotiate better prices from drug manufacturers and hospitals—but just keep those savings as profits for themselves.

Vertical integration could also reduce competition through exclusivity. Consumers could be harmed if, say, CVS refused to fill Humana policyholders' prescriptions, or Walmart charged Aetna customers higher prices. This may seem hypothetical, but regulators care about hypotheticals. In November, the Department of Justice sued to block another vertical merger—AT&T's proposed acquisition of Time Warner—over concerns that the integrated company would withhold their shows from other internet providers and cable companies.

Healthcare is ripe for a shakeup. Soon Amazon drones may be delivering prescriptions, Walmart doing blood tests, and CVS providing urgent care. Let's hope the Trump administration regulators are ready.