PHARMACY AUGUST 2011

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Editorial

The casualties from the wounds inflicted to traditional retailers (including pharmacies), failing to respond to changing customer behaviour continue to mount. The Australian retail morgue now include Borders, Colorado, Angus & Robertson, Krispy Kreme, Perfume Empire and numerous independents, while the casualty ward carries wounded icons such as David Jones, Harvey Norman, Myer, fashion chains and of course community Pharmacies proving that all retail sectors are being impacted.

However consumers are continuing to spend – it is just that some of that spend is now through different channels and retail alternatives which have exposed single channel "Bricks and Mortar" retailers. Smart retailers are embracing a multi-channel approach while the innovative single channel online retailers grow rapidly in number and continue to generate huge sales growth. This trend is self-perpetuating as

1) Global and local economic climates pressure consumers to chase maximum value for their spend

2) Consumers can source an endless range of merchandise

3) Time spent buying is slashed thus enhancing convenience and

4) Manufacturers/retailers respond to reduced sales volume by selling stock for extraordinarily low prices online for both promotional reasons and the need to reduce excessive inventory levels.

Large National retailers' silence is overtly conspicuous as they actively try to avoid publicly promoting the presence of on-line competitors (eg Kogan, Catchoftheday, Spreets, Scoopon etc) who are strongly influencing customer expectations as well as their view of the value offered by "high street" retailers.

In a recent BRW article the creator of online retailer Catchoftheday, Gabby Leibovich was reported as saying "Australia has so much growth to go. In the US and UK its (online retailing as a percentage of total retail spend) closer to 10%. And the price spread between bricks-and-mortar and online here is the widest in the world - estimated to be 40%. Something's going to have to give."

Meanwhile social media (eg Facebook, Twitter etc) is also playing a role in shaping Digital consumers' expectations of what they now expect when interacting with a retailer (refer Bruce's article) while the growing "Green" consumer group prefer retailers who satisfy their expectations of corporate behaviour regarding environmental responsibility.

So why are retailers (especially Pharmacy owners) unable, unwilling or slow to adapt their model and customer offer in response to these tectonic shifts in customer behaviour and preferences?

While reasons are numerous, legitimate excuses are difficult to find. Regardless, adaptation to remain relevant and viable is critical and requires planning to develop a complete new pharmacy business model which extends beyond customer 'service' through to customer 'engagement' (as service is insufficient by itself). This can only be achieved via multiple channels including in-store whole of pharmacy commitment to this vision, investment and ultimately acceptance, that what has served so well historically will not in the future produce the same success.

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JRx pharmacy
Level 30, Central Plaza One 345 Queen Street Brisbane Qld 4000
GPO Box 1144 Brisbane Qld 4001 Phone (07) 3222 8444
Fax (07) 3221 7779 www.jr.com.au/pharmacy

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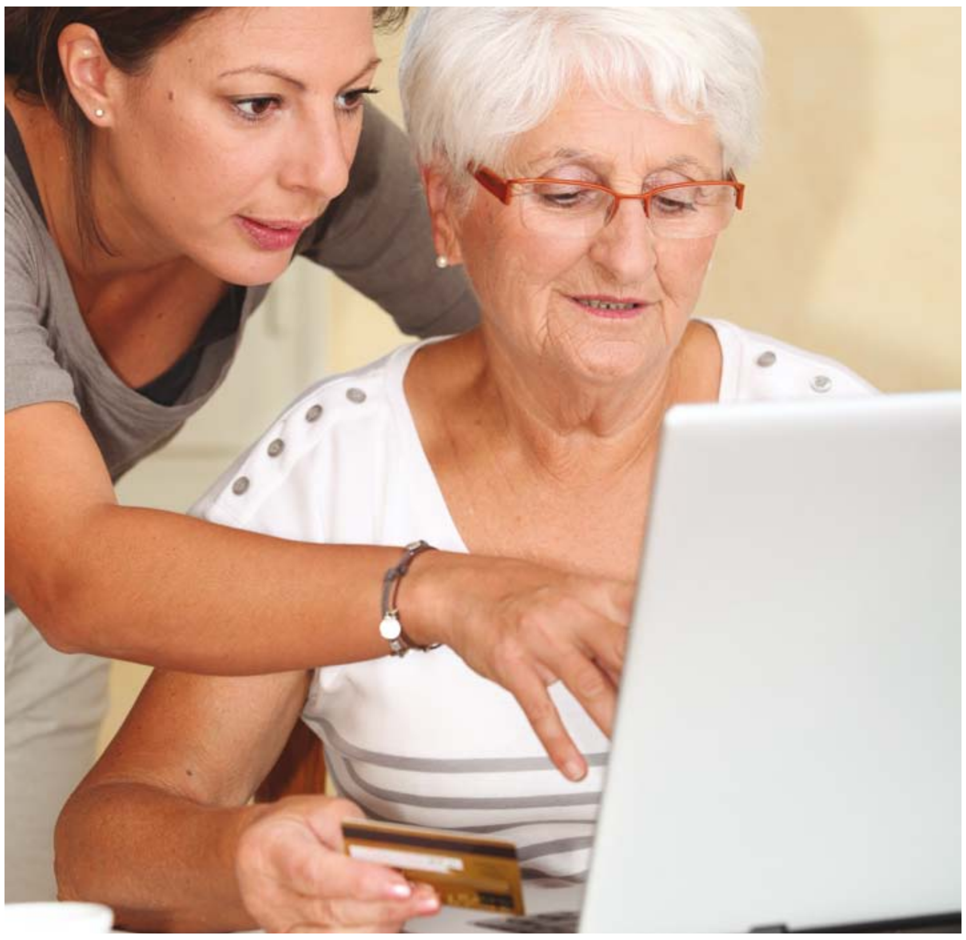

In the face of a changing competitive landscape, single channel 'bricks and mortar' retailers, including pharmacy, are rapidly losing market share. Returning to growth and long term prosperity means changing fundamentals on a number of levels - differentiation (via cost leadership or quality enhancement), coherent stock mix that supports a unique health solution proposition, a layout that enhances the customers in-store experience and offers multiple channels that engage customers (ie: online, iPhone app, social media, catalogue, loyalty programs (meaning CRM and not just a discount program) and standard media).

To highlight the risk associated with not arresting stagnation, financial success for a shopping centre Pharmacy translates to approximately $5,000 gross profit per sqm (ie at 33.3% GP then turnover of approx $15,000 per sqm). This point is not well understood by many owners and groups and particularly shopping centre landlords who are now for the first time being confronted with faltering pharmacy tenants. And of course if rampant and deep price discounting is the only response to competition, customers buying through alternative channels, plateauing script volumes and declining retail sales (and hence GP$) the increased sales per sqm required to hold up the bottom line becomes virtually impossible. Clearly something has to give on both sides of this equation.

Further exacerbating the position though is Pharmacy's approach to reporting shopping centre turnover by including only non PBS receipts thereby ensuring landlords don't see the true picture. (Problematically though I doubt it is actually possible to uniformly change Pharmacy preferences to report lower turnover figures and thereby reduce what is presently a distorted and artificially high rent percentage of sales benchmark). Ultimately, market forces in the wider retail arena have to exert downward pressure on rents but this should not be viewed as a given nor a solution. In the meantime some owners are now deciding to shift out of high rent shopping centres while others are selling.

Equally, the issues discussed above are not isolated to shopping centre pharmacies alone. Assessing formats, management reporting systems, services, categories and customer interaction is an ongoing challenge for all retail businesses. Adaptation and innovation within a changing environment ultimately defines those who are successful. The articles in this edition by Bruce, Teresa and Norman provide further commentary, ideas and insight about how to start or enhance your pharmacy's customer engagement in a rampantly changing environment.

Enjoy ! – Mark Nicholson

Discounting - pharmacy is not alone

I recall sitting here in July 2010 looking out into the 2011 financial year with the same optimism as I do today. The only difference is the last 12 months may have been the worst retail conditions we will see for some time – or are they? The question that now needs addressing is what will change in 2012 to improve the situation?

During the first half of last financial year the national press were not discussing how flat the economy was. This view changed in the last quarter of FY2011 and recently retail CEO's such as David Zahra of David Jones have commented that the conditions are the worst in 20 years. In the last month Zahra suggested that David Jones was in fact in the 'perfect storm', a comment we have previously attributed to pharmacy given heightened competition, the shift in customer spending behaviours and for pharmacy, Pfizer's move and the consequences of price reductions in the dispensary that are yet to be felt in their full form.

Statistics from the ABS suggest retail sales growth for May 2011 compared to May 2010 was up 2.6%. Growth was supposed to be 8.6% in pharmaceutical, cosmetic and toiletry retailing on the same month last year which is surprisingly strong. We know that the PBS expenditure was tracking at about 5% growth for the period ended June 2011 (note volume was about 2.5% for the same period) which means that the difference is coming from the health and beauty components of pharmacy and supermarket and general retail. Interestingly, this analysis holds true for each of the preceding months during 2011.

Where is the growth coming from?

JR Pharmacy client base category averages for the six months to June 2011 suggest total retail customers and sales increased 5% and 2.9% respectively. Specifically, the following categories achieved the growth:

	Cust # Growth	Sales $ Growth
Cough/Cold	17.78%	16.04%
Scheduled Medicines	25.96%	16.63%
Diabetes	19.42%	25.95%
Eye Care	5.43%	11.14%
First Aid	9.07%	6.55%
Home Healthcare	16.79%	12.18%
Sinus & Allergy	8.47%	(4.20)%
Digestion	6.47%	5.12%
Vitamins & Nutr.	15.34%	16.19%

While the following categories experienced negative growth during the same period:

	Cust # Growth	Sales $ Growth
Family Planning	26.83%	22.75%
Quit Smoking	10.90%	9.76%
Weight Management	10.20%	18.86%
Baby	3.94%	5.23%
Prestige Cosmetics	3.87%	23.10%
Gifts	14.66%	14.66%
Photographics	22.57%	34.78%

The price of discounting

The surprise in the data to June 2011 is the decline in GP$. Despite sales growth, GP$ fell 2.95%. This highlights the number of pharmacies now discounting in an attempt to lift sales and customer numbers. I accept there is a need to be competitive but the question has to be considered whether this strategy is effective in achieving customer and profitable growth.

Reflecting on the David Jones position, department stores are not the cheapest so they must do something different (the brand of brands) – but are they? The recent June stocktake sales have yielded little for the department store. Sound familiar?

Discounting fuels commoditisation of product. What has happened in the last few years is the price of many products in pharmacy have reduced across the board and now all pharmacies are making less profit from these items. It is a deathly spiral.

Consumers are still spending – the numbers tell us that. It is where they are spending that matters. Consumers are looking for something different that offers value (value = price + quality) – the opening of Zara in Sydney and Melbourne has demonstrated this to the department stores.

To return to profitable growth hard decisions are required. There is growth in the pharmacy sector but it is not wide spread. Decisions need to be made not only regarding the mix and quantity of stock in the pharmacy but the delivery of tangible services that support the categories and stock carried. Businesses achieving growth develop momentum through continual change driven by opportunities identified from targeting customer needs.

It is this culture that breeds success. These types of pharmacy businesses :

- Do the basics well by limiting overhead waste;
- Use category data to work out what customers are buying (or are not buying);
- Are never out of stock in what customers want;
- Reduce/remove what they don't want (refer category data above);
- Always have the pharmacist hand out the script;
- Implement government funded programs in the pharmacy that can be commercialised and create a point of difference in the customers' eyes;
- Implement and benchmark a system whereby customers are provided a solution (as opposed to a complimentary sale);
- Benchmark their results at pharmacy and category level and use the data.

By doing the above you will make it easier for a customer to use your pharmacy. Aim to provide an effortless experience that is unique – reduce waiting times, increase the number of options for customers to transact with you, increase the touch points for marketing including using tools such as the internet and facebook etc while also highlighting new products to customers (ie don't just put it on the shelf).

Going for growth means creating change. Not making change is fatal.

- Norman Thurecht

Customers check my prices, get advice and buy elsewhere

'You laugh at me because I'm different. I laugh at you because you're all the same' – Lady Gaga

Customers drive the pharmacy agenda now more than ever and they are using alternative channels to buy traditional pharmacy lines. So it is no wonder I am commonly asked: 'What can I do about customers who come into my pharmacy to check my prices but then leave to buy elsewhere, usually at the warehouse pharmacy or online?' And some customers don't even bother coming in now as buying online means they don't have to!

Digital flight to price

Smart phones are accelerating this behaviour as customers check range, availability and price of competitors then thrust their phones forward to prove why they deserve a discount. This behaviour will gather more steam as the digital and smart phone revolution drives the flight to price harder and faster. 46% of mobiles are now smart phones, compared with 31% in 2010, and expected to be 60% next year.[1]

Today 90% of smart phone searches ends in action and 74% who use them to shop proceed to purchase.[2] Research also says that price is the fifth reason Australian consumers use overseas online sites to buy, lagging well behind the two most important reasons—range and ease of finding product.[2]

This is no passing fad driven by the two-speed economy - meaning that pharmacy owners can not get through by discounting for a while and then whacking prices back up later. The revolution in customer shopping habits will continue because its soul is found in convenience (saving time) rather than lowest price.

Take a look at one Australian warehouse pharmacy group which offers customers five, so far as I know, channels to access their offer and buy:

1) Bricks and mortar stores
2) Web site (on-line) including on-line catalogue
3) Catalogue
4) Radio station
5) iPhone application – search, buy, compare, click and collect, reminders etc.

The real competitive grunt is the interconnection of all the channels providing a synergistically powerful retail offer that reaches more customer groups utilising a concept called 'cross channel retailing'. Research has proven that the more channels you have to reach customers and patients with, the more competitive your offer and the higher your average sale will be. If you want more information please email me at **bannabel@jr.com.au** and I will send you some material.

Pharmacy reaction inadequate - hastening commoditisation

The point is that customers use alternative channels to save time, know/find the lowest price and, hence, visit traditional bricks and mortar stores and shopping centre precincts less. Unless you have something special and valuable to offer, excessive discounting in an attempt to lift customer value will continue driving your margins, net profit and valuation into the ground. It's not sustainable.

Selling cheap is easy and it seems the only department escaping devaluation is PBS dispensing, which should hold up for the next three or so years thanks to generics as pharmacists aren't permitted to discount PBS. So pharmacy owner response thus far has been diametrically opposed to what they should be doing. Ie: lifting quality to increase customer value instead of cutting price.

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In effect community pharmacy owners should blame less the pricing policies of warehouse, supermarket and online competition and instead look at their own reaction that simply plays into competitors hands and only continues the downward spiral in a game they will not and cannot win.

Answering the question

The starting place in lifting the quality of the customer offer is to be found in addressing the uncompetitive out of date pharmacy business model by first considering the following critical future success points:

1) Renew focus on the in-pharmacy experience from the customer perspective, not yours
2) Deliver on the health 'brand' promise starting with pharmacist role and dispensary
3) Embrace multi and cross channel retailing
4) Connect and leverage social media

For community pharmacy viability the focus must be quality health service solutions, deep health ranges, information, problem solving and sharing. By comparison the warehouse focus is on widest range and lowest price. Put another way warehouse pharmacy is competing in a different market with a different business model compared with community pharmacy.

The key is to enhance the customer's experience (point 1), which is why I wrote my June 2011 AJP article 'Low rate cuts both ways' that proposes valuing a pharmacist time and expertise depending on their contribution to the customer's experience.

Community pharmacy does not just have to be about (and can't afford to be about) lower price, pretend discount and convenience dispensing, with a bit of advice tendered from time to time when deemed suitable or there is time. Consider the customer's perspective and the experience your pharmacy offers them compared with the rest. Maybe Lady Gaga is right!

The pharmacy and pharmacist who puts the customer first and lifts value by offering and delivering the highest quality customer focussed 'health' brand are doing well. Subscribing to only the first two points they have positioned themselves above the pack, including getting rid of redundant features, replacing them with skills and value-adding strategies (including stock mix) that matter, they are achieving double-digit growth.

Some of these are now moving into points three and four with positive results that proves the customer market demand is already there! One pharmacy has gathered over 1,500 script customer email addresses to improve script management (reminders, repeats, pay and check scripts held, buy related recommended health products) via the pharmacy web site and send them health relevant information via Twitter. Another pharmacy has over 4,000 Facebook customers interacting. The catchcry for the place of social media (such as Facebook and Twitter) utilisation in pharmacy is 'customers bringing customers'.

'If you're not on the web and cannot be found your business simply is invisible.'[3]

So perhaps without an active social media strategy your business will have fewer customer/patient conversations and your message may not be heard.

Pharmacist/customer engagement

We already know improving stock mix quality results in sales increases as it reinforces the customer's perception about what the pharmacy actually stands for. The same can just as easily be applied to improving the quality mix of staff skill-sets offered to customers.

For the past 12 months I've worked with Glenn Guilfoyle of The Next Level, an expert systems time and motion specialist, who late last year analysed dispensary effectiveness (as opposed to process efficiency) in pharmacies throughout Australia.

He proved that the average health-related product sale was significantly greater when the pharmacist/customer engagement was high. The health-related average sale per customer for the traditional pharmacies was around $4. Yet pharmacies that always had a pharmacist at the front, not bogged down in script assembly and who engaged the script customer on more than 80% of occasions achieved in excess of $9. The actual difference was $5.08 and these pharmacists who were focussed on improving customer health (as opposed to companion selling) said they had only scratched the surface!

This is about health-related products that enhance customer health and/or enhance efficacy of the medicine dispensed. Further, anecdotal evidence suggests that their customers also enjoy the experience and interaction with the pharmacist (points 1 and 2). The message therefore is to Build margin dollars through customer engagement and never forget delighted customers will bring you customers!

Valuing the engagement

Focussing on two of the pharmacies Glenn analysed, we see this approach impacting on whole-of-pharmacy performance well above industry average growth and profitability.

Compared with same period last year, customer numbers were up 7.4% and 12%, gross margin holding at 36.3% and 36.2% (ignoring the few customers who want to pay less) and net profit/sales (EBIT) of 16.1% and 12.5% respectively. Yet they started with the same traditional pharmacy model as everyone else but worked for two to three years on improving quality.

For more detail on the financial justification of employing and/or freeing additional customer hours please refer to my July 11 AJP article 'driving the customer experience'.

A good day isn't just about dispensing 300 scripts (profitability of which will shrink) as much as it is about helping 100 people stay well or get better. So make a decision to stand for something different and valuable, and then deliver it. That will give customers reasons to 'stick' and not slip away to the lowest price product purveyors.

– Bruce Annabel

1) A C Nielsen
2) Paul Marshall. Salmat. Turning disruption to advantage. Online Retailer Roadshow. Brisbane 3 June 2011.
3) Kate Conroy, product specialist Google. Without the web you're invisible. O Angel. Australian 20 July 2011 page 33.

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Teresa Hooper – Partner
Direct: 3222 8461
Email: thooper@jr.com.au

Mark Nicholson – Partner
Direct: 3222 8434
Email: mnicholson@jr.com.au

Bruce Annabel – Consultant
Direct: 3222 8401
Email: bannabel@jr.com.au

Norman Thurecht – Partner
Direct: 3222 8316
Email: nthurecht@jr.com.au

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