BUSINESS

FEATURE | BUSINESS MODELS

So you want your business to succeed…

KEY POINTS

- Focus on the foundations of location, size and rental rate before considering how to re-brand your pharmacy.
- The owners' visions and values are critical to developing a new business model, as are their leadership and management skills.
- Successful change requires developing a unique selling proposition, commitment, dollars and, ultimately, acceptance that what has served so well historically will not succeed in the future.

RE-ENGINEERING A PHARMACY BUSINESS MODEL TO SUCCEED IS A TOUGH BUT CRITICAL DECISION IN THE FACE OF INCREASING COMPETITION AND REDUCING MARGINS WRITES **MARK NICHOLSON.***

It has often been said that operating a retail business is simple, but achieving success is not easy. Most pharmacy owners I know would agree. The recent commentary reporting an increase in the number of pharmacy owners being in financial distress only serves to reinforce this point further. And this has occurred prior to the impact of the yet-to-be-felt 1 April price cuts!

This article is the first of a two-part series that considers the determinants of a successful pharmacy business model. It will be followed in next month's *AJP* when my business partner Norman Thurecht considers the various brand offers available to pharmacy owners and their key points of difference.

But branding is only one piece of the complex structure that forms the business model and which underpins a successful pharmacy. While many pharmacies begin with this as a starting point, it should in fact only be decided upon once other foundations have been laid.

LOCATION, SIZE, RENTAL RATE

During 2011, a client was confronting a difficult negotiation with a shopping centre landlord where, in my consideration, he had too much space, was in the wrong part of a shopping centre, and the per square metre rate was excessive compared to other tenancies. Such a triple whammy is not an uncommon situation and usually happens because of a variety of reasons including:

- **a brand group has negotiated for the site and then matched an owner to it;**
- **the pharmacist has owned an existing site in the centre and is not prepared to have a competitor take a new second site; and**
- **it is a 'Greenfield' site without goodwill costs and, due to high demand, a landlord has a number of competing bidders prepared to commit to the site.**

In each of the above circumstances the negotiation process is skewed towards the landlord, and when this occurs, it is more likely than not that too much space will be taken and the rate will be towards the maximum end of the market range. If this occurs, then regardless of the brand the owner goes with (independent or banner) and the capabilities of the owner, the main beneficiary is likely to be the landlord.

While the importance of location and site size is critical for a shopping centre pharmacy, it also ultimately dictates the success of strip and medical centre pharmacies. For each type of business, proximity to customer traffic and volume of potential customers are critical determinants of how much space should be taken as well as the rate per square metre. Even warehouse pharmacies apply this principle by choosing high road traffic flow locations with good parking, even though they avoid high rent positions next to supermarkets.

Only after these decisions are made should the question of what brand be considered. Often (and with potential financial detriment to an owner) a space commitment is made based on the brand preference rather than identifying the optimal space for the site. Consequently, most brands that have larger standard formats also have underperforming pharmacies in their group.

To reinforce the risk associated with oversizing, financial success for a shopping centre pharmacy translates to a minimum of approximately \$5,000 gross profit per square metre (ie. at 33.3% GP then turnover of approx \$15,000 per sqm). This point is not well understood by many owners and groups, nor (and especially) shopping centre landlords who are now, for the first time, being confronted with faltering tenants.

Equally, this issue is not isolated to shopping centre pharmacies. Assessing formats, together with management reporting systems, services, categories and customer communication, is an ongoing challenge for all retail businesses. Adaptation and innovation within a rapidly changing environment ultimately defines those who succeed.

The remainder of this article explores these components and their contribution to what many owners currently seek: a successful pharmacy model for the future.

OWNER'S VISION AND VALUES

As noted above, good pharmacy businesses are always well located and usually have the appropriate amount of space at the right price. The hallmark of a truly great business, however, lies with the owner's ability to define a strategy and then pursue it relentlessly.

To carry on the initial theme of this article, many understand that business strategy may often be simple in theory but not easy in practice. The below key components in the strategic planning process require understanding, defining, communication and buy-in from all stakeholders.

Vision: the future view of what the owner wants the business to be (eg. a leader in community healthcare).

Mission: what the business does to achieve its vision (eg. deliver innovative services, programs and professional support to improve the use of medicines and patient health outcomes).

Values: shared beliefs of owners and staff. Ultimately it is the values that underpin a business culture and ability to achieve its core purpose.

Unfortunately and in my experience, most pharmacy owners do not formally and rigorously work through this process and commit their thoughts to paper, communicate them with staff and then relentlessly pursue their stated goals. Given the challenges the industry faces with ongoing price reductions via the government's weighted average disclosed pricing (WADP) mechanism, warehouse and supermarket competition and a depressed retail environment, I believe future growth can only come from well-defined and clearly executed strategies.

Achieving this requires equal parts of both leadership and management. They are very different skills and can be defined as:

Creating monthly disciplines that involve reporting, reviewing and action will create a platform for continuous improvement

Leadership: setting direction or developing a vision.

Management: controlling or directing people and resources with reference to the values so as to achieve the vision.

SYSTEMS

Like all businesses, the systems employed by a pharmacy will provide the foundation for efficient management and timely feedback for strategy assessment and ongoing improvement.

Systems are available for branding, category management, payroll, book keeping, financial reporting, staff training, human resources, walk the store, stock management (POS) and so on. Historically though, most pharmacy owners have been able to achieve growth and manage their business without the use of electronic systems (dispensary and POS aside)—and where they do exist, with the bare minimum of analysis utilising system reporting functions.

Creating monthly disciplines that involve reporting, reviewing and action will create a platform for continuous improvement.

BRANDS: AN OUTSOURCED SYSTEM

Independent pharmacies in Australia are fortunate to have a broad range of choices should they want assistance in branding their business.

These franchise opportunities (which will be discussed in more detail in the next issue of the *AJP*) are not 'turn-key' solutions, but instead offer services that are consistent with, and complement, the defined mission, vision and values of the business. Good brands have scale and leverage not available to a single pharmacy operator and should be able to provide services and skills not normally within reach of small business.

Ironically and despite paying for these varied services, many owners do not regularly and actively engage their franchisors for assistance beyond catalogue distribution, despite most offering fee-inclusive assistance for services such as marketing, remerchandising, category market data, staff training, store assessments and so on.

Importantly, the ability to outsource branding should provide an owner more time to focus on both leading and managing areas such as clinical services development and implementation which, in most people's view including mine, can be the differentiator to both drive growth and protect margins well into the future.

BRANDING: GOING IT ALONE

For many pharmacy owners, the decision to join a recognised brand and comply with their various requirements is deemed too onerous or too expensive. Often though, the underlying reason is an unwillingness to change or invest in the change process.

The only valid reason that I can see for not outsourcing the branding function, however, is that the owner can do it better. For this to occur, an owner must be willing to develop competencies and systems to deliver a better outcome for the pharmacy's customers.

For example, this may translate to a preference to do more multi-channel (website, email, Facebook, Twitter, smartphone apps) marketing and communication with customers and less catalogues. It may also include employing category management analysis to develop differentiated categories with specialised products supported by specialised skills, programs and services.

Pharmacies that make these choices are in fact choosing to develop their own brand. And by using their own data and market awareness of their local community, they are able to develop stronger connections with their customer base. This route is significantly more difficult than brand outsourcing but often more rewarding.

The two brand strategies raised

above—outsourcing versus internally managing—are not, however, mutually exclusive and can be blended depending on the outsourced brand's agreement. Every owner should consciously consider and decide what is most appropriate for their business and their market.

CUSTOMERS

Of course, a vision and strategy will only be successful if it meets customers' needs and wants. In recent times many retailers (especially pharmacy owners) have been unable, unwilling or slow to change their behaviour (and as a result their offer) in response to customer's rapidly changing behaviour and preferences.

Reasons are numerous but successful change requires planning to develop a unique selling proposition (USP), commitment, dollars and, ultimately, acceptance that what has served so well historically will not produce the same success in the future.

In the face of a changing competitive landscape, retailers (pharmacy and general) are losing market share. Returning to growth and long-term sustainability means changing fundamentals on a number of levels: differentiation (via price or service leadership); stock mix to support a unique-selling proposition; a layout that reinforces a differentiated position and reaches out to the particular target customer segment; and utilising a multi-channel approach to communicate with customers (ie. catalogues, website, social media, loyalty programs, standard media).

SOLUTIONS AND SERVICES

The continuing pressure on margins from WADP measures and supermarket/warehouse/internet competition has intensified the need for community pharmacies to develop a USP. To date, there has been broad recognition by industry leaders, professional organisations (including brands) and pharmacists that providing health solutions and professional services is central to developing a meaningful differentiated offer.

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The Pharmacy Guild of Australia's 'Roadmap Matrix' provides a good starting point for pharmacies to begin constructing their own USP. It provides various templates which are split between internal (ie. the dispensary, professional services area and consultation area) and external (ie. outreach health services and programs) areas.

At JR we actively encourage our clients to 'pick the low-hanging fruit' first and, as confidence grows, then expand their offer. Two examples are:

1. **Outsourcing DAA packaging. This can both free up resources and allow for scalable growth. Benefits include increased patient medication compliance and increased loyalty to the pharmacy with their script fulfilment. This requires some up-front workload to educate patients but is repaid in a short time.**
2. **Recording clinical interventions. All pharmacists make interventions and most on a daily basis. With payments for the recording of interventions, together with the ability for the Guild to use the data to prove the profession's value in the healthcare continuum, it is surprising that so many pharmacies are yet to commence.**

We see many other examples where our clients are successfully delivering a category solution and significantly increasing average sale along the way. Categories include scheduled medicines, weight management, diabetes, asthma and sleep disorders.

To be successful, though, generally requires changing the dispensary layout and often includes employing a non-dispensing pharmacist during busy periods who can actively consult with patients.

SUMMARY

Successful businesses are defined by their ability to adapt to a changing environment. They develop, implement, review and evolve their strategies in response to customer needs. They have systems that support staff and strategy management, and provide feedback about customer needs and wants. They view market disruption as an opportunity, not an obstacle.

The current remuneration framework allows the industry to continue to be both viable and successful in the long term. This does not, however, translate to all owners. Owners with high levels of debt and/or rent will face significant difficulties if the profit loss from WADP cannot be replaced by growth initiatives.

For many pharmacies, the short-term response to the market disruption caused by price cuts is to increase generic substitution. This is entirely appropriate but also one-dimensional and has a finite life. Brands are important, but only one piece of the jigsaw and should not be confused with being a successful business model in their own right.

A lasting response requires developing a new business model which, in turn, requires a different approach to:

1. **the dispensary;**
2. **premises area, layout and design;**
3. **merchandise mix and category specialisations;**
4. **staff levels, mix, skills and engagement to deliver services;**
5. **open and active communication channels to the market; and**
6. **management systems.**

But the final and most important message is: owners are, and will always be, their business' main determinant of success or failure.

** Mark Nicholson is managing partner of JT Pharmacy Services. E: mnicholson@jr.com.au*