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Dare to be different

COMMUNITY pharmacy can't employ a low-price strategy as the way to compete with sophisticated retailers such as Woolworths and the genuine low-price/cost pharmacy operators.

As I explained last month, community pharmacy must compete on convenience, top quality retail format, value-added healthcare product categories with expansive range and specialist services focused on patient health outcomes.

Pricing power of Woolworths

The Woolworths value proposition (method of attracting customers) is heavily dependent on three aspects we see and one that we can't. The three visible aspects are convenience, low prices and promotion (largely product/price). However, most importantly, it's behind the scenes where we find the key to Woolworths' ability to run a low-cost retail model. These include systems, data management, logistics/distribution, technology utilisation, product sourcing and top retail management skills.

Here are some examples as reported in *The Australian* (18 March 2004):

- AutoStockR—automated inventory and store ordering system. Stock outs and inventories have both fallen and time spent checking shelves has halved.
- StockSmart—tells suppliers how much stock is required and when, and ties in with Woolworths' every day low-price (EDLP) strategy into supermarkets. Improved stock forecasting can help avoid the peaks and troughs triggered by high/low pricing strategies.
- Freight management—smoothing transfer of stock from suppliers through to distribution centres, which will be reduced in number from 31 to 11.
- Cross-docking—stock received is not stored but moved and sorted directly onto trucks for store delivery. Once at the receiving dock, product is moved directly from the trucks to the shelves.

Woolworths has adopted many of the Wal-Mart (biggest retailer in the world and inventor of EDLP pricing strategy) cost reduction strategies. Wal-Mart's market share of the US pharmaceutical OTC market already exceeds all other drug chain competitors.

How to compete

The Woolworths and Wal-Mart pricing strategy should demonstrate that competing on price is out of the question! To compete Australian community pharmacy must:

- find sources of differentiation;
- keep costs in line; and
- manage pricing effectively.

However, low-price driven pharmacy retailers have altered consumer expectations about how much of the above they must trade off for low prices. The traditional community pharmacy approach to business and consumers that has worked in the past (maximise script throughput, minimise spending/buying and relying on political protection provided by the Guild as a given) will leave pharmacy in an extremely susceptible position.

So, community pharmacy can't play the low-price game because of its limitations in being able to reduce costs. Additionally, the service levels and premises rentals in pharmacy are much higher than supermarkets and some of the other new entrants into the market. Accordingly, more value must be created using what these higher costs provide: expertise, service/s, convenience, enjoyable shopping experience, accessible/easy-to-get-around format, and merchandise comprising a wide range of products in key value-add healthcare categories that consumers want to buy from a community pharmacy. Your point of sale (POS) reports will provide that information if you know how to analyse the data.

Most of these products, particularly S2/S3s, are not price sensitive! Certainly consumers don't think they are. Consumer research conducted recently by Roy Morgan Research disclosed that price only ranked seventh out of nine criteria when buying pharmaceuticals.

Regularly analysing pricing and using different approaches to prices is the way to recover money given away through crazy discounting, misguided price wars, lack of an effective pricing policy and blindly delegating the retail pricing task to pharmacy assistants not sufficiently trained in retail price management.

A case in playing the price game

Our 2003 client base averages for overheads/sales percentages were 23.6 per cent and gross profit percentage (GP%) was 32.7 per cent, leaving net profit margin of 9.1 per cent. Retail GP% including discounts and rebates was 38 per cent.

In contrast, one of our clients decided that they wanted to significantly reduce OTC prices to drive higher volume and, thus, overcome the margin percentage given away. Results showed retail GP% of 29 per cent (including discounts), total GP% of 28 per cent and sales growth in the last two years of 30 per cent and 14 per cent. This seems okay on the surface, but overheads were 25 per cent of sales due to comparable staff and rent levels that left net profit of only 3 per cent —insufficient to fund the refit lease and pre-existing debt levels. Clearly the model doesn't work because the whole strategy and retail pricing was misguided.

Playing the price game is foolhardy for the great majority of pharmacy retailers because the great majority of consumers buy on convenience and value, not price.

Community pharmacy must change by daring to be different and start taking advantage of the fantastic opportunities that are available for smart operators. ■

The views contained in this column are those of the author and not necessarily held by the AIPM

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