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PHARMACY SERVICES

What are your risky dollars?

DISPENSARY gross profit percentage (GP%) or margin is falling, as most of you are aware. Many pharmacists constantly complain about this 'dreadful' situation, but my reply is usually 'hey, that's great!'.

My reasoning is that the high-cost drugs, which are pushing up drug inflation and thus reducing margins, provide greater remuneration in terms of the gross profit dollars (GP$s) earned. Provided script numbers keep growing, so will the GP$s earned from the dispensary.

The key message is to focus on growing and monitoring GP$s whether they're generated by dispensary or retail sales. GP$s result from both the gross margin percentage (GM%) extracted (resulting from mark-up) and, most importantly, unit sales volume. Unfortunately most pharmacy owners are totally obsessed by the former and, hence, often sacrifice higher dollars in the chase for higher margin percentage.

Focus on dollars, not percentages

The Pharmaceutical Benefits Scheme (PBS) statistics tell us that the Federal Government PBS costs are increasing by a little under 9 per cent, driven by doctors prescribing higher cost drugs, while prescription numbers are growing by less than 2 per cent. That is, the PBS statistics support our client data that dispensary GP% has continued to fall this year.

But, that's okay for pharmacy because of the remuneration deal struck in a succession of agreements between the Federal Government and the Pharmacy Guild of Australia. Just to remind you, here is the remuneration structure for PBS prescriptions:

Dispense fee $4.66
Mark-up on wholesaler cost +10 per cent
(Maximum $18 on items costing up to $450)
(Then +4 per cent > $450)
Plus wholesaler discounts and generic incentives.

The key element is the +4 per cent mark-up on drugs costing in excess of $450 that ensures pharmacists continue to be well remunerated for the high cost drugs, which cost more to stock and maintain.

Consequently total pharmacy GP$s and net profit dollars (NP$s) have continued to rise in recent years even as the GP% has continued falling as evidenced by data from the Guild Digest (Table One).

In the meantime the dispensary GP% has continued sliding (by 4.7 per cent in the last five years) as reflected in our JR Pharmacy Services client base statistics.

Therefore, GP$ growth in the pharmacy has been driven by a combination of script growth, new high cost drugs and the PBS remuneration structure that provides higher dollar earn on higher cost drugs.

The lower margin drugs provide the highest dollar earn despite the lower margin percentage! Of course, pharmacy managers will need to manage stock ordering carefully to avoid out-of-date problems.

Reduce PBS dependence

Another conclusion legitimately drawn from the above analysis is that community pharmacy is heavily dependant on income generated from PBS prescription dispensing and the Community Pharmacy Agreements. Our 2003 client base statistics show that only 30.5 per cent of total sales were generated from non-prescription dispensing sources, that is, retail sales including pharmacy-only and pharmacist-only lines. So with negotiations about to start for the Fourth Community Pharmacy Agreement it is worthwhile looking at the sensitivity of pharmacy net profit in response in small changes to dispensing remuneration.

If we assume that there is, for example, a $1 reduction per script (equivalent to approximately 3 per cent) in the gross selling price resulting from adjusting any or all of the remuneration structures including the fee, wholesaler mark-up, pharmacy mark-up and generic 'incentives' let's look at the impact on NP$s of three different pharmacies (Table Two).

The outcome is alarming and reflects the high risk involved in pharmacies that erroneously discount retail prices, fail to regard non-prescription healthcare categories as core business income earners and don't run their dispensaries efficiently. And this is what I think the Federal Government will be looking at pharmacy owners to implement.

So, the dollars being earned today may soon become the risky dollars of tomorrow, or at least next year! ■

Table One

Year	GP$ Growth	Script no. growth	NP$ growth
2000	9.9%	7.2%	23.6%
2001	10.3%	7.2%	20.1%
2002	9.9%	4.7%	16.4%

Table Two

	Pharmacy One (000)	Pharmacy Two (000)	Pharmacy Three (000)
Total sales	$5,185	$2,081	$3,780
Retail sales proportion	33%	50%	28%
Total GP$s	$1,344	$804	$1,261
Retail GP%	27%	40%	38%
NP$s loss	($109)	($32)	($82)
NP% loss	(35%)	(12%)	(15%)