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JOHNSTON RORKE JR PHARMACY SERVICES

# When the price isn't right

MANY pharmacies are unnecessarily giving away margin (money) in the mistaken belief that customers won't deal with them unless prices are low. This obsession with selling for less is hanging like the sword of Damocles over the current and future profitability of community pharmacy.

This is a common theme among 90 per cent of new pharmacy clients coming to JR Pharmacy Services. These stores demonstrate retail gross profit margins of less than 30 per cent (including discounts and rebates). Many aren't even aware and are shocked when they find out.

Our client base average retail gross profit margin is higher than 38 per cent and some achieve in excess of 40 per cent! That's because we constantly focus our clients' attention on maximising prices. If your overall gross profit margin is less than 30 per cent, chances are that is caused by unnecessarily low retail prices.

True, several low-price pharmacy retailers have emerged. True, some of these retailers have sustained these low price retail offers but only because they run a genuine low-cost business model (a comparison in the airline industry can be made between Virgin and Qantas).

True, some low-price community pharmacies will fail because their operating costs are too high and they depend on the high profits currently generated from Pharmaceutical Benefits Scheme prescriptions. That won't last!

True, some pharmacies are located in markets where the consumer demographic dictates price as a more important issue than in other markets.

True, more people are buying on price as the sole motivator. But they represent only a very small minority of the total population. So why not pursue the remaining very large majority?

True, pharmacy retailers are making a rod for their own back by conditioning consumers to wait for discounts and expect low prices. The exceptions will be those running low-cost business models.

Trying to compete on price won't work for the traditional pharmacy. That's because the operating overheads as a percentage of sales (24 per cent) are much higher. According to my client base, the major expenses include wages (13 per cent) and rent (3.8 per cent). Fit-out cost (approximately $1,000/m2) is very high and, due to the relatively fragmented nature of the industry, product purchase costs are also higher.

Compare these with pharmacies operating a low-cost business model with total overheads at about 14 per cent of sales including wages (8 per cent) and rent (1 to 2 per cent). Fit-out costs are also much cheaper.

These inconvenient, low-service and comparatively spartan format environments carry large volumes of merchandise in large floor space (600m$^2$). This acknowledges that some consumers will trade away convenience, less service and ambience in order to get the low price. But, the low price must be an every day low price, apply to all merchandise and be at least 20 per cent below all competition.

That's the test of sustainability! There's always someone who can sell it cheaper.

Therefore, how can traditional community pharmacies compete with these other retail models if price is a fast track to Death Valley?

The answer lies first in recognising that most community pharmacies can't beat the true low-cost operators by competing directly. So, recognise right now that Woolworths, Priceline, and others who can deliver low-cost pharmacy models will always beat traditional community pharmacy on product sourcing, supplier partnering, systems, data utilisation, logistics/distribution and, hence, price.

### Consumer store selection

But, it's still possible to succeed as a community pharmacy by understanding why consumers shop at a pharmacy compared with other retail options. Store selection is driven by:

**1. Location:** Convenient, excellent layout and design relevant to the store offer, accessible internally and externally (visibility, parking), appealing/attractive, uncluttered, quality fixtures and fittings, internal and external signage and overall ambience.

**2. Merchandise range:** Meet the demand of consumers in the particular market area of that pharmacy. Selected key/signature categories that create a statement or image of what the store is about and differentiates it from the low price operators and all the other 'me too' pharmacies. It is essential to build on the offer by adding specialist services/knowledge that focus on consumer outcomes rather than just the usual product at a price pharmacy has become accustomed to. Be consistent!

**3. Price:** If prices on all products are 20 per cent or more cheaper than all other competitors some consumers will trade away or forsake location, specialist merchandise range and service attributes.

Therefore, pharmacy can compete by differentiating. This means concentrating on doing 'location' and 'merchandise range' extremely well rather than simply saying they do and hiding behind regulation! Ultimately consumers will determine community pharmacy success.

My next article will elaborate more on the price issue, discuss what Woolworths and Wal-mart (the world's biggest retailer) are doing with price and how specialist pharmacy retailers can and do compete successfully. ■

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

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