Pharmacy Values hold while Earnings Risk Increases ?

The multiples applied to Pharmacy earnings to calculate a sale price have not fallen despite the reality and continued risk of falling remuneration – why we may ask ?

The signing of the 4th Guild Government Agreement late last year should have signalled some certainty to owners about the next four and a half years. However, the ongoing issue of generics and other incomplete matters such as the location rules (still being finalised with Government) provide anything but certainty.

Add to this increasing product pricing pressure from competition (both within the industry and from supermarkets), rising overheads (ie rent and wages), a reduction in scripts per patient being written by a static number of GP's and potential interest rate rises (albeit small) and the combined result is anything but rising future income levels.

You could be forgiven for thinking that none of these underlying changes are being considered by buyers, and financiers of pharmacies! After all, pharmacy values are a function of their future earnings. (As a quick summary - earnings are capitalised into a value using a capitalisation rate. This value represents equipment, fittings, stock, NHS number with the balance being goodwill.)

So given a purchaser paying goodwill is buying the net present value of the future earnings, what happens if these _future_ earnings are under threat? In a fully informed in-balance market, values would adjust to reflect increased risks. Pharmacy though is not necessarily balanced – i.e. supply = demand.

The contributors helping to maintain pharmacy values is the limitation of new NHS numbers and the restrictive location rules which will be largely preserved under the new Guild Government Agreement.

The result - it remains a sellers market and 'buyer beware'.

Until the Government via its clandestine Interdepartmental committee decides whether they will reduce remuneration by tweaking generics and/or wholesaler's discounts (or the Guild can slay the dragon), significant risk exists with current profit levels remaining for the term of the new Agreement.

By way of example, should the Government take on further generic margin clawback, it has been estimated that the net profit of pharmacies could fall by between \$30,000 and \$50,000 on average. Assuming a metropolitan capitalisation rate of 18%, the value of a pharmacy should fall by \$170,000 to \$280,000 overnight. What actually results in the market would depend on buyer perception regarding individual pharmacies.

The clear message here is that some of the risk fundamentals have increased yet Pharmacy prices remain as high as ever. The intergenerational transfer of pharmacy ownership will continue and industry debt levels will continue to rise. Prescription remuneration growth cannot be relied upon to offset rising costs. Other growth strategies must be implemented and certainly must be considered well before any contract is signed for the purchase of a new pharmacy.