Success in the Pharmacy Channel

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Introduction

Pharmacies represent a potential sales channel for both life sciences companies and fast-moving consumer-goods (FMCG) companies. However this channel differs from other traditional channels (surgeries and hospitals for life sciences companies, and supermarkets for FMCGs) in many ways, and needs to be carefully managed if a success is to be made of it.

For life sciences companies, pharmacies represent a highly profitable alternative to the traditional GP and hospital channels in which to sell medical devices and drugs. As a general trend, healthcare provision in both the public and private sectors is evolving significantly as providers pursue cost containment measures. Buyers are adopting a more sophisticated and price-sensitive approach, purchasing centers have a stronger role within hospitals, competitive tenders are increasingly important, generic providers are gaining market share and new communication technologies represent both opportunities and threats for the manufacturers. These changes force life sciences companies to review their sales strategy in order to preserve their profit margins.

For FMCG companies that offer food & beverage and personal care products, pharmacies represent an additional high potential channel. In most European countries, the proportion of pharmacy sales comprising these products is increasing significantly. For example, the sales mix of these categories in Italy represents 12% of total pharmacy turnover and it is growing year on year. The profitability of the pharmacy channel across Europe as a whole is even higher; the average margin for the manufacturer being 30-55% of the consumer price. Finally, para-pharmacies, which sell the full range of products sold in the pharmacies but not prescription drugs, are also growing rapidly in number. In some European countries, the number of para-pharmacy stores has increased 10-fold between January 2007 and 2010.

Although life sciences and FMCG businesses have already developed a product portfolio that is suitable for the pharmacy channel, some of these companies still do not consider pharmacies as a viable opportunity. This is because there are significant challenges to successfully exploiting the channel in addition to the usual challenges to driving sales in other channels. In some countries, including Italy, the pharmacies are highly fragmented with very few consolidated buying groups, chains or distribution agreements. Pharmacies also require a high service level – orders placed today must be delivered within 24 - 48 hours – and customers typically order small quantities, causing high logistics costs for the manufacturers. In addition to this, pharmacy store managers and owners in certain countries have their share of business legally guaranteed as a certain proportion of the population. This can mean that they are less proactive in reaching out to consumers.

However, on a positive note, potential pharmacy business is evolving: the proportion and mix of non-pharmaceutical products is increasing rapidly, making it an ideal time to consider new ways of approaching customers. Deep knowledge of the channel, combined with a carefully structured approach, can secure effective entry into the pharmacies market and support highly profitable operations.

Critical success factors in the pharmacy channel

If both life sciences and FMCG companies are to succeed in the pharmacy channel, they need to rely on a specific blend of those critical success factors (CSFs) which characterize success in the traditional consumer and healthcare markets. As in the consumer markets, it is crucial that businesses set the right price, determine the optimum level of trade spending, select the correct product mix, run strong advertising campaigns, provide good customer service and an effective sales force. As in the healthcare markets, it is important that both pharmacists and specialists have clear information and see the added value of the product over competitors. It is also crucial to understand the customer potential in both markets and to invest resources in building long term relationships where that potential is highest.

Life sciences and FMCG offer a wide variety of products in pharmacies. These include drugs provided by life sciences companies, which can only be sold with a prescription from a GP or specialist, plus over-the-counter (OTC) self-medication products from FMCG businesses. FMCG companies also offer more functional food and personal care products in the pharmacies. Table 1 shows how the significance of the CSFs can vary depending on the type of product under consideration. However, it is not only the product and service attributes that bring revenue for life sciences and FMCG businesses (price, quality, delivery, and the marketing thereof). It is also the coherence and effectiveness of the commercial strategy – such as accurate segmentation, targeting with the right portfolio and information, efficient and right-sized sales forces, plus good planning and implementation – that brings success to the pharmacy channel across all of these product categories.

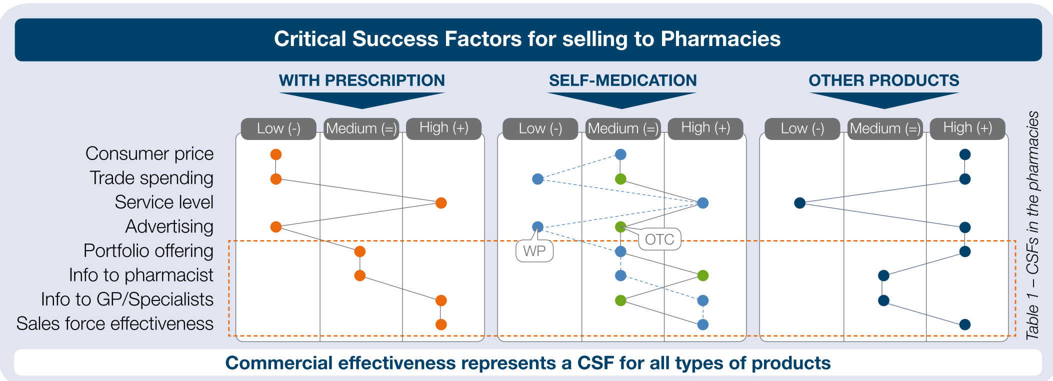

Table 1 – CSFs in the pharmacies

A structured approach

Experience of supporting life sciences and FMCG to enter and maximize profits in the pharmacy market shows that there are five main phases in developing and implementing the required strategy:

1. Product portfolio definition and market analysis;
2. Pharmacies segmentation and targeting;
3. Sales force sizing and route to market identification;
4. Route to market selection and business planning;
5. Implementation.

1. Product portfolio definition and market analysis

The first phase of the entry strategy is to identify the product portfolio with the highest potential for that channel. This can be done within the existing R&D and marketing processes of the company but should also take into account the special characteristics of the channel.
In particular, the products should add real value not only to the final customers but also to the pharmacists. These professionals are keen not only to maximize profits (product rotation, price and trade discounts are the key target indicators) but also to reduce the management complexity of their suppliers (service level plus contract terms and conditions are the main target indicators here). Due to the evolving nature of consumer expectations when it comes to the sort of products that they want to buy in pharmacies, this should not be a one-off definition but an ongoing activity. For example, consumers are increasingly opting to buy healthy foods, nutrition-related products and other consumer goods from their pharmacist. To support this new product mix, pharmaceutical companies also need to develop their marketing approach in tandem, drawing on traditional FMCG methods, such as product promotions and merchandising.

It is in this phase that a detailed market analysis should be conducted to define the medium and long term potential for the company. The analysis should consider the key trends in the market, the competitive arena and the value attributes in which the industry is investing. The targeted output of this phase will be the best product portfolio for the pharmacy channel and its market potential over the medium to long term.

2. Pharmacy segmentation and targeting

The second phase is to segment and target the pharmacies effectively. This phase is crucial for maximizing profits from the channel and great emphasis should be placed on accurately calculating pharmacy potential. The problem is particularly acute in highly fragmented markets where companies will only see big returns by focusing on the highest potential pharmacies and must invest heavily to develop strong relationships with them. Even if market research companies offer data on the topic, careful attention should be invested in customizing these generic indices to the core product categories of the company. This requires specific algorithms that consider critical factors distinctive to the company in question, as well as general market databases. For instance, for a company selling skin products, the algorithm might increase the potential of those pharmacies that are located next to dermatology clinics and hospitals.

Once the true pharmacy potentials have been calculated, these should be segmented into clusters on that basis. The appropriate visit parameters and activities can then be selected for each segment, the guiding idea being that the highest potential segment receives the greatest investment. The output of this phase is segmentation on the basis of potential, along with specific visit frequencies and durations, activities and investments.

3. Sales force sizing and route to market identification

Once the pharmacies have been segmented and assigned the appropriate visits, the company can size its sales force accordingly. This can be done by comparing the total number of hours needed on a yearly basis to cover the segments with the determined number and duration of visits, against the total number of hours available on a yearly basis per FTE. This comparison results in the total number of FTEs required. The calculation is theoretical and does not take into account geographical constraints. For instance, if the assigned territories are too large then the salesman will be spending more time in the car and accordingly less in the pharmacy. However, factoring in these sorts of constraints can deliver a clear definition of the size of sales force needed.

Having sized the sales force, the company needs to identify the best route to market. There are at least four choices here. The company can take a direct route to market, meaning that all reps are either employed by the company or are fully dedicated sales agents. Taking this option is comparable to using third party logistics operators for distribution. Given the significant fragmentation of the pharmacy market in countries such as Italy, it may not be optimal or even feasible to manage deliveries within the company's own logistics network. Alternatively, the company could work via wholesalers, meaning that it does not employ its own sales force and the distribution is managed by third parties. These wholesalers may also perform commercial activities such as direct mailing or training sessions. A third option is to work with dealers, whereby the sales force is managed directly by a third party that also manages distribution (in some cases the dealer in turn may use third party wholesales and logistics operators). Finally, the company could outsource its sales operations. Whichever option the company takes, it is vital to recognize that they cannot serve fragmented pharmacy markets in the usual way. To deliver such a high service level and such small quantities is usually too costly to return a healthy profit. Of course, a company might also decide to take a tiered approach, adopting one solution for its biggest customers and another for the lower potential segments.

The output of this phase is the required size of the sales force and a description of the alternative routes to market, along with detailed options.

Deep dive: developing an efficient sales force

There are two main levers when developing an effective and efficient sales force for the pharmacy channel: territory coverage and visit management.

Many companies invest a lot of resource and effort in maximising their coverage of the territory and the number of pharmacies that they sell to. In fact, territory coverage is best analysed in terms of market potential rather than number of pharmacies. To see why, consider the Italian pharmacy market. In Italy, there are more than 17,000 pharmacies which can be grouped into three broad clusters. There are the 3,000 largest pharmacies which constitute 40% of the market. Then there is a second tier of 5,500 medium-sized pharmacies which make up another 40% of the market. The remaining 8,500 smallest pharmacies represent just 20% of the market.

Other things being equal, the sales force should focus most attention on the first cluster and then the second, whilst the third tier might be covered by dealers or wholesalers. Assuming that companies apply the same visit parameters to pharmacies (typically frequency and duration), conduct the same activities and make the same investment for every pharmacy covered, then it will be more effective to link the effort to the potential of the pharmacy. So, sales forces should visit the higher potential pharmacies more frequently, and for longer, than they do the other pharmacies and the activities that they undertake at the stores should be adapted accordingly. Investment plans should also be aligned to this targeting, with more money invested in in-store activities, merchandising, point-of-sale materials and training for the high potential pharmacies. The guiding principle is that there is a direct link between pharmacy potential and the revenues a business can earn from it and, equally, there should be a direct link between these revenues and the business' level of investment.

PHARMACY

4. Route to market selection and business planning

The alternative routes to market identified above have pros and cons that must be carefully considered in light of the specific needs of the business (Table 2.).

When selecting the best route to market, businesses should consider quantitative aspects as well as the qualitative ones. In other words, all costs (both fixed and variable) and benefits must be identified and processed to build a P&L on a multi-year horizon for every type of route to market. Through this sort of business planning it is possible to calculate the ROI of the venture and choose the route to market accordingly.

Routes to market	Pros	Cons
Direct	■ Greater control over commercial strategy and execution ■ Strong sales pushing in all high-potential pharmacies (e.g. in-store activities, ECM courses, etc.)	■ High fixed costs ■ Low rate of field force utilization ■ Heavy internal structure to handle invoicing or extra costs to externalize it ■ Credit risk not externalized
Wholesalers	■ Small administrative burden ■ Credit risk externalized to the wholesalers	■ Low or absent sales pushing in-store (not suitable especially when launching new products)
Dealers	■ Strong sales pushing in all high-potential pharmacies (e.g. in-store activities, ECM courses, etc.) ■ Small administrative burden ■ Credit risk externalized to the wholesalers and dealers	■ Potential overlapping with private label products ■ Potential conflict with product priorities of agents (agents push products with the highest turnover)
Outsourced sales force	■ Sales pushing in all high-potential pharmacies (e.g. in-store activities, ECM courses, etc.)	■ Questionable commercial effectiveness (low loyalty, high turnover of sales agents) ■ Sales activities and distribution not connected ■ Credit risk not externalized ■ Heavy internal structure to handle invoicing or extra costs to externalize it

Table 2 | Pros and cons of the alternative routes to market

5. Implementation

The last phase of the project approach is about implementing the business plan. It involves:

- Drafting a detailed implementation plan (activities, owners, tools and milestones);
- Developing the product portfolio (including possible R&D activities);
- Upgrading the internal processes and organization (some professional roles may be missing in the company and the in charge of the pharmacies must be developed);
- Scouting and selecting the potential partners (wholesalers, dealers and third party field forces).

It is normally best for implementation to be executed through a dedicated PMO so that management do not lose focus on their current business.

The following table outlines the overall project approach.

Overall approach to the pharmacy channel

	Product protfolio definition and market analysis	Segment pharmacies & target	Sales force size & routes to market	Select route to market; build business plan	Implement
KEY ACTIVITIES	▪ Identification of the **best product protfolio** for the pharmacy channel ▪ Analysis of the **market data and trends** ▪ Assessment of **market potential**	▪ Assessment of the **market potential** of each pharmacy ▪ Segmentation of the pharmacies into **homogenous clusters** in terms of market potential ▪ Assignment of the **visits frequency and duration** target to each cluster	▪ Based on segmention and targeting, **sizing of the sales force** ▪ Identification of the **alternative routes to market**	▪ Assessment of **pros and cons of** the identified alternatives ▪ Definition of the **key hyptheses** in terms of benefits and costs ▪ Developement of the **5-year pharmacy channel and consolidated P & L** ▪ Selection of the **most effective and efficent route to the market**	▪ Design of the **launch plan** in terms of: ▪ Main project **streams** ▪ **Key activities** ▪ **Timing** ▪ **Owners** ▪ Upgrade the **internal process, organization** and **product portfolio**
KEY ISSUES	*What is the best product portfolio and what is ist market potential?*	*What are the pharmacies in which to invest the most?*	*Which is the correct sales force size to target them? Which are the possible routes to market?*	*Which is the best route to market? What are the projected economics?*	*What are the next steps?*

Table 3 | Overall project approach

What can be achieved?

Companies that apply this approach rigorously can reap great rewards. For example, in a recent partnership between Tefen and a global medical devices company, the company was able to overcome margin erosion in its traditional hospital channel and, by tackling the pharmacy channel, increased profits by one third.
The business had been facing serious challenges in many major European countries. In some cases more than 80% of their total revenue came from the hospital channel, in which potential sales and margins were in decline due to fierce price competition and cost containment policies from the NHS. The remaining 20% of revenues already came from pharmacies, but this was under threat from a competitor launching a new product with the same active ingredient but not requiring a prescription. Moreover, many other competitors were strengthening their presence in the pharmacy channel, stealing market share and capitalizing on synergies and spill-over effects from their presence in the hospital channel.
In order to reverse this decline in market position, sales and margins, the company sought to assess the potential of the pharmacy channel and define a successful entry strategy. On the basis of the structured approach described in this article, the company is now on track to grow revenues by 25% and operating margins by 33%, as part of a 5-year growth strategy.
As we have seen, there are big rewards available for companies exploiting the pharmacy channel. However, the competition is already on the playing field and employing aggressive tactics. A customized and structured approach is the only way to successfully capture a share of the rewards and forge ahead of the rest.

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