

Growth Drivers: The Factors Behind Independent Pharmacy OTC Sales

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in partnership with



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The Factors Behind
Independent Pharmacy OTC Sales

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Executive summary

In October 2011, Hamacher Resource Group (HRG), the Healthcare Distribution Management Association (HDMA) and the Consumer Healthcare Products Association (CHPA) released a white paper titled *Supply Chain Collaboration: Maximizing Health, Beauty, and Wellness Product Sales in Independent Pharmacy*. This original research revealed six non-prescription product categories that performed better in independent pharmacies than in their chain drug counterparts. The paper further discussed healthcare trends poised to have an impact on the drug retailing industry. It also offered action items for consumer healthcare product manufacturers, distributors, and retailers, based on exclusive interviews and in-depth research with each of these segments of the retail consumer healthcare supply chain.

Supply Chain Collaboration identified the following six front-end categories as evidently outperforming in independent pharmacies versus chain drugstores:

1. First Aid
2. Eye/Ear Care
3. Sun Care
4. Smoking Deterrents
5. Incontinence/HHC/Diabetes
6. Foot Care



HDMA's Health, Beauty and Wellness (HBW) committee then posed a series of follow-up questions:

1. What dollar amount is associated with each of the sales increases indicated for the six categories?
2. What were the subcategories that evidently drove growth in each of the top performing categories?
3. In contrast to these top performers, what categories underperformed in independent pharmacy when compared to chain drug, and why?
4. How have these same categories increased or declined over the past three years, and why?
5. What related purchases were associated with these six core categories?

The following pages will divulge additional analysis and insight into what factors help stimulate growth in the categories that are driving the independent pharmacy front-end.

Key insights

Along with offering previously unavailable analysis, this research reveals the following insights.

- Independent pharmacy captured a \$22 million increase within four key categories.
- The composition of categories favors medicinally-focused items in independent pharmacies.
- Market basket increases can be attributed to companion items and category adjacencies.
- Cold & Allergy and Pain Relief are among the underperforming categories in independent pharmacy.

Research methodology

Portions of this study were compiled through review of healthcare distributor warehouse withdrawal data for the 24-month time period between January 1, 2009, and December 31, 2010. Categories were analyzed individually to determine dollar sales growth. Syndicated data from SymphonyIRI Group for food, drug and mass outlets was also analyzed to provide a point of contrast with independent pharmacy.

Digging into the data

A percent sales increase in a category is news worth noting. Increased sales and profitability are the lifeblood of any retailer. They hold more significance in the independent pharmacy marketplace because even a modest front-end sales increase translates to more than the price charged for each discrete purchase.

The table below is reproduced and enhanced from *Supply Chain Collaboration* and shows the six front-end categories that grew at a more significant percentage in independent pharmacies than in their chain drug counterparts between 2009 and 2010.

	Column 1	Column 2	Column 3	Column 4	Column 5
Category	Percent \$ Sales Change 2009-2010 FDMX [†]	Percent \$ Sales Change 2009-2010 Chain Drug [†]	Percent \$ Sales Change 2009-2010 Ind. Phcy. [‡]	Dollar Amt Associated w/ Column 3	Ind. Phcy. Market Share Increase
First Aid	+5.29%	+6.31%	+16.45%	\$12 million	N/A
Eye/Ear Care	+4.44%	+5.28%	+10.71%	\$6.53 million	2009 = 8% 2010 = 9%
Sun Care	+9.56%	+10.16%	+10.17%	\$0.85 million	N/A
Smoking Deterrents	-0.16%	-2.40%	+8.34%	\$2.93 million	2009 = 8% 2010 = 9%
Foot Care	-3.09%	-3.50%	-0.75%	N/A	2009 = 4% 2010 = 5%

[†] As derived from analysis of SymphonyIRI Group syndicated data for the period January 2009 through December 2010.

[‡] Based on distributor warehouse withdrawal data for the period January 2009 through December 2010.

Incontinence/HHC/Diabetes comprises multiple categories that cannot be separated for analysis and as such has been omitted from this table.



Using the First Aid category as our example, we can examine and reasonably estimate what a \$12 million annual increase in sales through independent pharmacies means on an individual store basis.

Sales of \$12 million spread across a population of approximately 20,000 independent pharmacies equates to \$600 per year, per store. Of course a \$600 annual per-store increase does not by itself create a more profitable outlook, but consider what factors lay behind that \$600.

At an average price of \$6 for a first aid item, \$600 translates to approximately 100 additional front-end purchases per year, per store. Now consider how frequently a first aid purchase might be combined with a purchase from a complementary category, such as pain relief or surgical wound care. Rather quickly, the potential for 100 \$6 purchases multiplies to 100 opportunities for a total market basket of \$25 or more. Instead of an opportunity for first aid sales of \$600 per year, an independent community pharmacy now can welcome the very real possibility of an additional \$1,875 in sales per year, driven solely by a percentage increase in sales in the First Aid category.



Successful subcategories

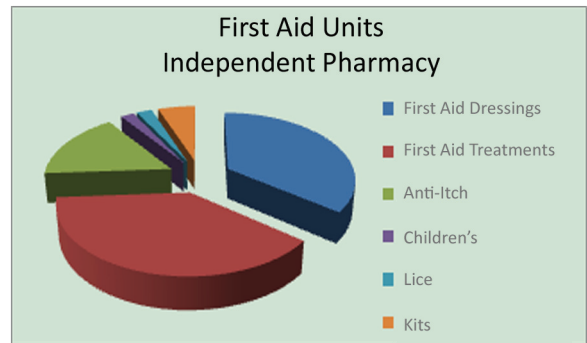
The six high-performance categories in independent pharmacies identified in *Supply Chain Collaboration* comprise related subcategories that, when analyzed separately, reveal what types of purchases are driving category growth. In many cases, this deeper analysis also reveals interesting contrasts between consumers’ preference for particular subcategories in independent pharmacies versus chain pharmacies. The story that unfolds indicates that consumers tend to favor independent community pharmacies for medicinal or clinical-type purchases, but chain pharmacies for healthcare items that might be considered more mass-market.

Shown below in sales of units, we can see that the First Aid Treatments subcategory drives sales in independent community pharmacies, while First Aid Dressings is far and away the unit sales leader in chain pharmacies. Community pharmacy sales data is derived from analysis of HRG’s exclusive wholesaler withdrawal data and chain drugstore data stems from data collected by SymphonyIRI Group.

The First Aid Treatments subcategory is composed of products including antibiotics, skin treatments, wound cleansers, and antiseptics.

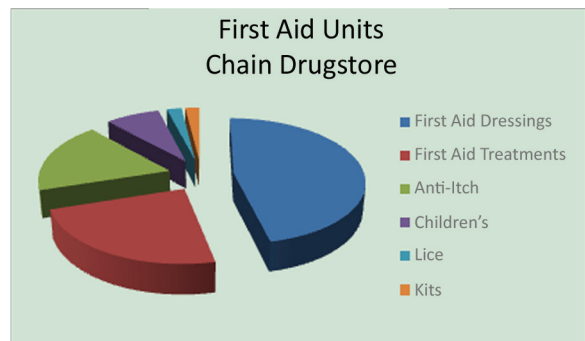
Independent Pharmacy

Subcategory	% Unit Sales
First Aid Treatments	38.39%
First Aid Dressings	35.58%
Anti-Itch	16.14%
Kits	5.53%
Lice	2.29%
Children’s	1.98%



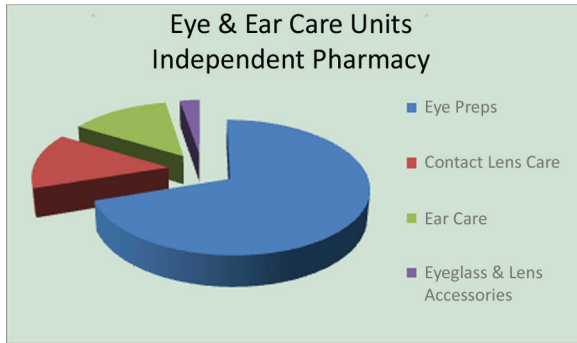
Chain Drugstore

Subcategory	% Unit Sales
First Aid Dressings	46.49%
First Aid Treatments	23.60%
Anti-Itch	18.12%
Children’s	7.70%
Lice	2.10%
Kits	1.99%



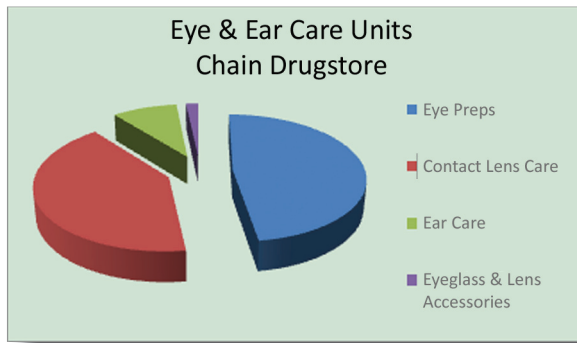
Similarly, the Eye Preps subcategory (primarily eye wash and dry eye relief) overwhelmingly drives unit sales within community pharmacies, while in chain pharmacies it is responsible for sales a full 20 percent less.

Even more significant is the difference between community pharmacies and chains in terms of Contact Lens Care product sales, with this subcategory pulling in 41.42 percent of unit sales in chains, but only 13.78 percent in independent community pharmacies.



Independent Pharmacy

Subcategory	% Unit Sales
Eye Preps	69.89%
Contact Lens Care	13.78%
Ear Care	13.64%
Eyeglass & Lens Accessories	2.69%



Chain Drugstore

Subcategory	% Unit Sales
Eye Preps	47.75%
Contact Lens Care	41.42%
Ear Care	9.13%
Eyeglass & Lens Accessories	1.70%

Other contrasts between the growth drivers in independent community pharmacies and chain pharmacies include the Smoking Deterrents category, in which patches dominate community pharmacy with 73.04 percent of unit sales, but sell only 23.06 percent in chain pharmacies, where nicotine gum tends to dominate sales. In Foot Care, Antifungal medicines lead community pharmacies with 37.69 percent of unit sales, but are responsible for 23.38 percent of sales in chains, where Insoles & Inserts dominate unit sales.

The underperformers

As in every type of retailer, the story in the independent pharmacy front-end is not all about robust sales growth. The categories listed below can be considered to have underperformed in independent pharmacies between 2009 and 2010 when compared with chain drugstores.

Category	Column 1	Column 2	Column 3
	Percent \$ Sales Change 2009-2010 Chain Drug	Percent \$ Sales Change 2009-2010 Ind. Phcy.	Dollar Amt Associated w/ Column 2
Cold & Allergy	-1.62%	-8.03%	(\$14.43) million
Oral Care	+14.26%	-2.62%	(\$1.39) million
Pain Relief	-0.81%	-20.20%	(\$18.81) million
Vitamins/Dietary Supplements	+8.99%	+1.47%	\$1.83 million

The typically front-end leading categories of Cold & Allergy and Pain Relief are most notable among these underperformers. In the case of Cold & Allergy and Pain Relief, both chain drugstores and independent pharmacies experienced a loss due to product shortages and availability challenges.

Sales growth in these top three “headlining” categories — where Rx-to-OTC switches dominate product sales — is quite often driven by national promotions initiated by major brands. Coupon and rebate offers tend to benefit chain drug and mass retailers more than independent pharmacies, where opportunity exists to increase cooperation with brand-led marketing efforts. Independent pharmacies also can benefit from a thorough audit of these front-end departments to ensure that major brands and popular products are double-faced when possible, and that out-of-stock conditions are not detracting from sales.

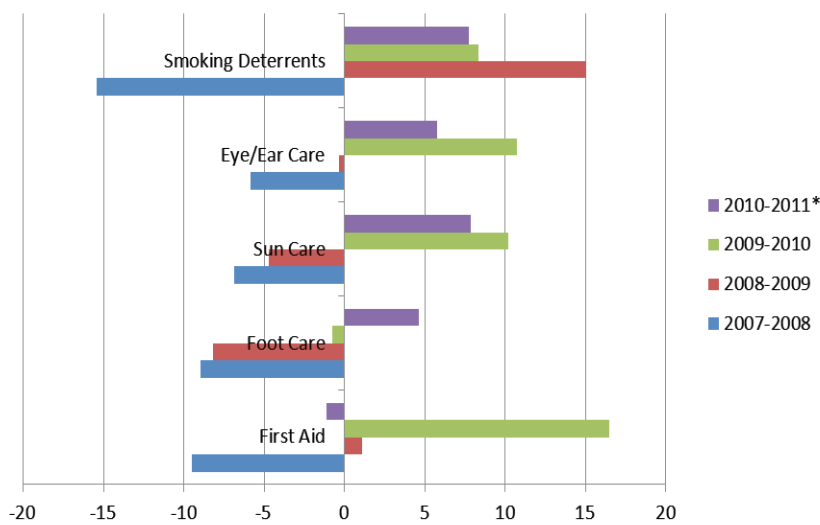
Trends over time

Between 2007 and 2010, the six categories under scrutiny fluctuated between growth and decline within the independent pharmacy retail segment. The chart presented below summarizes the relative sales growth or decline, based upon warehouse withdrawal data obtained and analyzed exclusively by HRG.

Virtually every category shows a similar trajectory. The calendar year 2008 showed a major decline in all of the categories. This decline is certainly consistent with the jolt felt throughout much of the economy as a result of the recessionary period which began in the latter part of 2008. At the same time, the decline is consistent with a similar downward trend seen in independent pharmacy during the years 2006 and 2007. The modest uptick in calendar year 2009 and the virtual sprint forward in 2010 indicate an excellent recovery, at least for those time periods.

The longer term slide that preceded the 2010 growth spurt can perhaps be explained in large part by the effects of Medicare Part D on the independent pharmacy sector, effects which first reverberated in 2006 but continued to present a challenge for at least the first 18 months of the prescription entitlement program's existence. Confusion about eligible prescription plans, a difficult adjustment to longer reimbursement windows for prescriptions covered by Medicare and the new onslaught of chain drug competition in the form of \$4 generics was enough to distract independent pharmacies from maximizing the performance of their front-ends. The evident recovery of these six featured categories in 2010 is reason for optimism.

Category trends



* Reflective of sales through Q3 2011.

Growing the market basket

The first aid example from page four is a prime illustration of how a purchase from one key category can spur purchases from other categories to create a total “market basket spend” that far transcends the value of selling an individual product.

Understanding what categories’ products often appear in the same market basket with a given category is crucial to many aspects of independent pharmacy operations. Chief among them are store layout, or placing categories in logical relation to one another to encourage and simplify shopping. When it’s understood what categories consumers naturally shop together, setting up cross-promotions in-store becomes much easier and more successful.

In short, understanding the power of the market basket and companion sales can be as simple as studying customer behavior.

Category management research based on shopper behavior shows that products from the following categories often are purchased at the same time as the “main” category.

Main Category	Also in Market Basket	Why?
First Aid	Wound Care Pain Relief Home Health Care	post-surgical; limited mobility
Eye/Ear Care	Vitamins/Supplements	eye health
Sun Care	Skin Care Pain Relief Cold & Allergy (lip care)	sunburn relief
Smoking Deterrents	Gum and Mints Oral Care Vitamins/Supplements	fresh breath; “calming” supplements
Incontinence/HHC/Diabetes	Skin Care First Aid Home Health Care	skin protection
Foot Care	Skin Care First Aid Pain Relief	skin protection and healing

Common category adjacencies

Studying how customers navigate a pharmacy and analyzing what types of products they most often purchase during one trip is a first step toward maximizing shopper spending in the pharmacy front-end. Once a pharmacy's particular shopping patterns are understood, it is possible to encourage even more of the same behavior.

Arranging categories in the front-end according to logical shopping and purchase behavior has been shown to increase the size of the average market basket. The theory behind the practice says that shoppers will select more items for purchase if they are positioned conveniently. Secondly, locating complementary categories within line of sight increases the opportunities to catch the attention of customers who are shopping for related needs, but may not otherwise know to look in other categories.

The table below shares common category adjacencies for the six “outperforming” categories, based in part upon known market basket similarities as well as their inclusion of complementary products.

Main Category	Common Adjacencies
First Aid	Foot Care Incontinence Home Health Care
Eye/Ear Care	Vitamins/Supplements
Sun Care	Skin Care
Smoking Deterrents	Vitamins/Supplements Oral Care
Incontinence/HHC/Diabetes	First Aid Home Health Care
Foot Care	First Aid

Concluding remarks

Independent pharmacies have a host of opportunities to compete on more even footing with their chain drug counterparts. The first place to begin — in addition to reviewing *Supply Chain Collaboration: Maximizing Health, Beauty, and Wellness Product Sales in Independent Pharmacy* — is adopting more of the merchandising and in-store marketing practices that serve chains so well. Independent pharmacies can look to their distributors, manufacturer partners and business advisors as they seek to fill more consumers' healthcare needs with accessible, affordable, community-based care.

Acknowledgements

Thank you to the members of the HDMA HBW Committee for their continued commitment to enhancing the relationship between suppliers and distributors on behalf of independent pharmacies.

About Hamacher Resource Group, Inc. (HRG) www.hamacher.com

Hamacher Resource Group, Inc. is a full-service research, marketing, and technology firm specializing in retail consumer healthcare. Manufacturers, distributors, retailers, technology providers and others rely on HRG's 30-plus years of experience for solutions ranging from strategic planning through implementation. HRG is a WBENC-Certified Women's Business Enterprise headquartered in Waukesha, Wisconsin, just west of Milwaukee.

About the Healthcare Distribution Management Association (HDMA) www.HealthcareDistribution.org

HDMA is the national association representing primary healthcare distributors, the vital link between the nation's pharmaceutical manufacturers and healthcare providers. Each business day, HDMA member companies ensure that nearly nine million prescription medicines and healthcare products are delivered safely and efficiently to nearly 200,000 pharmacies, hospitals, long-term care facilities, clinics and others nationwide. HDMA and its members work daily to provide value and achieve cost savings, an estimated \$42 billion each year to our nation's healthcare system.

About the Consumer Healthcare Products Association (CHPA) www.chpa-info.org

CHPA is the 131-year-old trade association representing U.S. manufacturers and distributors of over-the-counter medicines and dietary supplements. CHPA is committed to promoting the increasingly vital role of over-the-counter medicines and dietary supplements in America's healthcare system through science, education, and advocacy. The association provides leadership and guidance on regulatory and scientific issues to Congress; state legislatures; and federal, state, and international government agencies. CHPA shares tools and information with partners across the globe to ensure the safe and responsible use of OTC medicines.