

Pharmacy Expansion

The how-to's, challenges and benefits of opening additional pharmacy locations

By Kathleen Barbosa

Summers Pharmacy, an independent community pharmacy in Clinton, Mo., had only been open a few weeks when a local hospital presented an opportunity.

Golden Valley Memorial Hospital contacted Ryan Summers, Pharm.D., co-owner of Summers Pharmacy, about opening a second location at its clinic. Another independent pharmacy that held the space for 20 years had just closed down, and the hospital wanted to replace it.

“The hospital, the clinic, the patients and the physicians were all used to having a pharmacy there,” Summers said.

The hospital was considering putting in its own outpatient pharmacy, and Walgreens was also looking into opening a location in the space, but Summers said the hospital wanted to know if he and his wife and co-owner, Julie Summers, Pharm.D., were interested first.

This seemed like an opportunity for Summers

Pharmacy to make a bigger impression on the community, to keep the physicians happy and to prevent competition from entering the clinic.

“We started looking at it and thought we could open one up and be successful,” Summers said.

Just four months after opening its original location, Summers Pharmacy opened the doors to its second location at the hospital clinic on Aug. 1, 2013.

“It wasn’t easy, but it wasn’t that bad either,” Summers said.

Opening an additional location can be beneficial for independent community pharmacies, but how do you know when, where, and if you should open another location?

Three independent community pharmacy owners share their insights into growing their businesses by opening additional locations.

HURDLES YOU’LL FACE

Opening an additional location presents no shortage of challenges for independent community pharmacy owners.

When starting out, independents can face shortages of essential elements, namely staff and capital.

“What prohibits many independents from opening up another store is probably staffing,” said Chris Schiller, Pharm.D., vice president

of operations at Economy Pharmacy, an independent community pharmacy with four locations in Oklahoma.

It can be difficult to stretch your current staff to fill a second location, so opening another location often requires hiring more people. The cost of the new staff, the physical location, the equipment and the inventory you’ll need, can add up to another common problem—capital.

Opening a second location requires enough cash flow to stay in business while you’re working to attract new patients.

“It takes a while to start making money from zero, especially with how much it costs to start up,” said Schiller, who has helped open two additional locations for Economy Pharmacy. “Independents have to have enough capital to be able to make it until they become profitable. That’s the biggest challenge.”

Geography created an additional hurdle for Schiller. He helped open Economy Pharmacy’s third and fourth locations in Tulsa, Okla.—an hour away from the two

other locations in Muskogee, Okla.

“Being in a new city, I didn’t know the doctors, and even though we’re not very far away, the cultures were a little different,” Schiller said.

For Summers, the location in the hospital clinic—in the same town as the original pharmacy—was ideal. It created access to new patients in the same community, and it helped the pharmacy build relationships with the hospital staff and with local physicians. But, there was a catch.

“The previous lease for the pharmacy there had got to the point that it wasn’t really beneficial to the pharmacy. It was pretty drastic,” Summers said. “So, obtaining a lease that was beneficial to the pharmacy and the hospital, and then getting a pharmacy manager to operate the pharmacy were our biggest challenges.”

When Koby Prater, Pharm.D., owner of Prater’s Pharmacy in Seneca, Mo., bought out the owners of Bruner’s Pharmacy in Webb City, Mo., he thought he was prepared.

“I planned quite a bit before we took control of it,” Prater said. But despite his plans, unexpected challenges emerged.

“A lot of things came up that weren’t foreseen,” he said. “The new pharmacy had

charge accounts that were out of control that we had to rein in. We’re still working on that and it’s been about six months.”

ESTABLISHING UNIFORMITY

Creating consistency is another challenge of owning multiple pharmacy locations.

Summers said he had to train the staff at his new location to adhere to the same procedures as the main location. “We obtained a lot of the same staff that the clinic location had previously, so some of them had to make some adjustments,” he said.

Prater had a similar situation. He said initiating new policies at Bruner’s Pharmacy took six to eight weeks, and even longer in some areas, because employees were used to the policies their previous pharmacist used for 30 years.

“The technicians weren’t being utilized to their full potential, so even though they had worked there a long

“I’m always looking for a good location and a good opportunity.”

Pharmacy Acquisition Financing Checklist

If you're looking to open an additional pharmacy location, make sure you've taken these steps before starting the financing process.

- ✓ Identify the pharmacy you wish to acquire. Identify a pharmacy that has a solid customer (prescription) base. Is there an opportunity to grow the business? Is this the pharmacy for you?
- ✓ Perform high level due diligence. Analyze the types of prescriptions being filled. Make sure you are comfortable with the product mix (controlled substance volume, durable medical equipment, compounding and workers compensation.)
- ✓ Determine the Net Operating Income (NOI) of the pharmacy. This is defined as income after all operating expenses are deducted from gross margin, but before income taxes and interest are deducted.
- ✓ Determine the value of the pharmacy. A pharmacy is worth what a buyer is willing to pay for it (in cash), or what a lender is willing to finance. It must produce a cash flow sufficient to repay the loan. Every situation is different, but lenders generally want to see at least 25 percent

more cash flow than is required to service the loan.

- ✓ Execute an agreement with the seller in writing, "Letter of Intent" or "Term Sheet." This outlines the terms and conditions related to the acquisition, executed with the assistance of your legal advisor or attorney. Ultimately, after the term sheet is executed, it will guide your legal counsel in creating the final purchase agreement.
- ✓ Obtain prequalification for financing. Get prequalified for a loan amount that will cover both your project development and working capital costs. You should feel confident knowing you have adequate capital to manage your business, and to repay your debt.
- ✓ Initiate the Asset Purchase Agreement with your attorney. With your tax planning arranged, you should consult with an industry-specific attorney to draft the purchase agreement.

Once you have followed the steps in this checklist, talk with your lender about your financing needs and the type of loan that will work best for you.

Courtesy of Jimmy Neil, general manager of the pharmacy division at Live Oak Bank

time, they basically had to learn their jobs all over and learn how to do a lot more," Prater said.

A SUBSTANTIAL INVESTMENT

Like all new ventures, opening a new location requires a financial investment. Looking at your current expenses can help you project what the minimum financial investment of opening a new location will be.

"I would estimate it costs at least six to 12 months of operating expenses," Summers said. "Just add all those first year expenses together and that's how much you're going to go into the hole essentially."

New licenses, insurance and contracts also have to be figured into the financial and time costs of opening a new location.

"It takes a lot of paperwork and time, getting all the forms and contracts filled out," Schiller said. "That's probably one of the biggest challenges."

For Prater, the time dedicated to training staff, attracting new business and addressing unexpected issues was the biggest investment.

"No matter what you think, you will be busier than you were," he said.

The physical site of your new location can also inflate your cost and time investment. "I like to have a hand in both places, but I can only be in one place at a time," said Prater, whose second pharmacy is about a 30-minute drive northeast from his first location.

Taking over Bruner's Pharmacy had its own set of financial challenges for Prater. "Initially, when we took over, they had a different computer system so we changed the software over, and changed the workflow around, and we also changed wholesalers," he said.

If you're unsure what level of time and capital you should invest, Prater recommends asking the experts to guide your investment.

"I have a good consultant who ran cash flow models for me and said we needed a certain number of patients and prescriptions," he said. This analysis helped him determine that it was feasible to take over the new

location, and it set benchmarks for how many scripts and patients the new location would need to be profitable.

Schiller, on the other hand, learned the challenges that come with leasing or building when he opened new stores for Economy Pharmacy.

"If you're leasing, you'll need your inventory, computer, and a build out, so you're talking probably \$400,000," Schiller said.

It took Schiller about six months to open a new location with a lease, and an entire year when the store was built from the ground up. "If you build a store from the beginning, you're talking a couple million dollars," he said.

Building and leasing each have pros and cons. With the leased store, Schiller was able to open a lot faster, but each month's rent cuts into profits. The custom-built store cost more upfront and took longer to build, but Schiller said designing everything exactly how they wanted was a big benefit.

GETTING NEW BUSINESS

No matter how much work you do ahead of time, one factor can make or break a new pharmacy location—whether or not you can get patients.

"When you open a new location and you're not purchasing a pharmacy that's already established, you start out with zero prescriptions," Schiller said. "The biggest thing is attracting new business."

And, attracting new patients to your new location—not just shuffling patients from your current location—is essential to success.

"Opening another location and taking patients from your first location to that location doesn't really benefit you," Summers said. "You're just adding costs to fill those prescriptions."

"We wanted to get extra prescriptions, so the clinic location was good for that," Summers said. "We were able to get antibiotics and pain medications, those sort of first fill medications that would have possibly gone to Walgreens or Wal-Mart."

"We're hoping that those first fills lead into more

future fills at either that clinic location or the main location,” he said.

But they didn’t just sit and wait. Summers said he marketed to new patients by sending out flyers and direct mailers to promote the new location.

“One of our new slogans we used for the second location was ‘two locations to better serve you,’” he said. Summers Pharmacy used the slogan on social media, on its prescription sacks and on advertising in the local newspaper.

Along with attracting new patients, Prater said one concern at Bruner’s Pharmacy was keeping current patients once he took over.

“In any ownership transition, it’s okay if the patients know it’s changing owners,” Prater said. “But hopefully you can make it seamless enough that they don’t even know there’s been a change.”

FACING THE COMPETITION

Whether your new location is in a familiar place or in a new city, you’ll likely face competition.

Prater’s main location in Seneca, Mo., is the only pharmacy in town, but when he took over Bruner’s Pharmacy in Webb City, Mo., he faced new competition from Walgreens, Wal-Mart, grocery store chains and other independents.

Despite the increased competition, Prater said he runs both locations the same way.

“I think it comes back to customer service in both locations,” he said.

Schiller said he thinks independents should actually consider opening a second location in an area where they’ll compete with big chains.

“I think there’s a good opportunity for independents, especially in a big city,” Schiller said. “Since I’ve moved from Muskogee, which had 38,000 people, to Tulsa, which is a much larger city, it’s easy to get business from chain customers. People are often intimidated by the chain pharmacies, but it’s actually a very good opportunity for independents.”

To determine if a second location is getting enough new business from the competition, Summers recommends setting and tracking goals.

“If the new location doesn’t hit the goals and timelines, you have to be willing to close it,” he said. “If

you’re not able to close it, you can’t risk opening it.”

Summers offered one key piece of advice to any independent pharmacy considering opening a new location in a big or small city.

“Be willing to compete, and if you’re able to take care of the patients, they’ll come to you,” he said.

SEEING THE BENEFITS

All this investment—the time, the money and the effort—can yield several business benefits.

Economy Pharmacy opened its first two locations in the same town of Muskogee, and Schiller said having two stores made it possible to go back and forth between locations to get patients the medications they needed.

“It’s such a huge benefit for inventory,” Schiller said. “If I don’t have something, my other store is probably going to have it.”

“When I opened our first store in Tulsa, it was the only store, so I was kind of at a disadvantage to the chain drug stores,” he said. “If I didn’t have something in stock, I couldn’t get it until the next day, but now that I have two stores in Tulsa, it’s a huge advantage.”

Prater’s Pharmacy found that adding another location meant better deals when ordering products.

“Buying power is one of the big benefits,” Prater said. “With common ownership, your revenue gets lumped together, so you get a better cost of goods.”

THE DECISION

There’s no simple metric that can tell you if you’re ready to open a second location, but you can learn from the advice of those who have done it.

Summers said pharmacy owners should consider where new prescriptions would come from before opening another location and to pay attention to patients’ attitudes, because they can signal an opportunity.

“You get a feel from the patients if they’re not being taken care of at other pharmacies,” he said. “If you’re getting a lot of transfers or hearing a lot of rumbling from patients, then there’s a way to get new patients.”

Even if there’s an opportunity, Summers said the main location has to be in good shape before you open a second.

“Don’t do anything unless your main location is running smooth and it can handle the owners, or the manager, being away from the main pharmacy during the

opening process,” he said. “You have to have things in order at your main pharmacy before you can open up a second location.”

For Prater, deciding to open a second location began by asking questions.

“Am I ready for this? Is this something that I really want to do? Do I have the time and the manpower to commit to doing this?,” he said. Prater said pharmacy owners should ask themselves these questions when deciding if they’re ready for the investment that a second location requires.

Schiller recommends learning more about your area’s population and demographic makeup to determine if your community can support another pharmacy.

“If there’s a town of 36,000 and there’s 14 pharmacies, they might not be able to support another one, no matter how much medicine they take,” he said.

LOOKING TO THE FUTURE

Once you open a second pharmacy location, you may find you’re always on the lookout for another opportunity. At least that’s how it is for Summers, Schiller and Prater.

Summers Pharmacy is already in the process of opening a third and fourth location. One of the acquisitions is still in the works, but Summers is in the final stages of opening a pharmacy in Butler, Mo.

“An opportunity just popped up a month or two ago to get into that community,” Summers said. “They had an independent pharmacy in town and a Wal-Mart pharmacy in town. I’ve never heard of this happening before, but the independent pharmacy owners just disappeared. They literally just walked away and left the community and patients high and dry.”

“I think that community likes having an independent pharmacy,” he said. “We want to get in there and provide that high level of service they’re used to.”

Prater and Schiller both said they don’t have any set plans for opening additional locations, but they’re not saying “no” to an opportunity either.

“I’m thinking probably in the next year or year and a half of opening up another location,” Schiller said. “I’m always looking for a good location and a good opportunity.”



Numbers to Know

Take a look at the trends for the average independent community pharmacy to see how your pharmacy compares.

27 – Percent of independent community pharmacy owners who have ownership in two or more pharmacies

1.71 – Average number of pharmacies in which each independent owner has ownership

8.3 – Average number of non-owner, full-time employees per pharmacy location

\$3,892,702 – Average annual sales per pharmacy location

62,424 – Average number of prescriptions dispensed per pharmacy location

Source: 2014 NCPA Digest (Based on data from 2013.)