

Metrics to Know

The numbers pharmacy businesses need to be measuring

By Kirsten Hudson

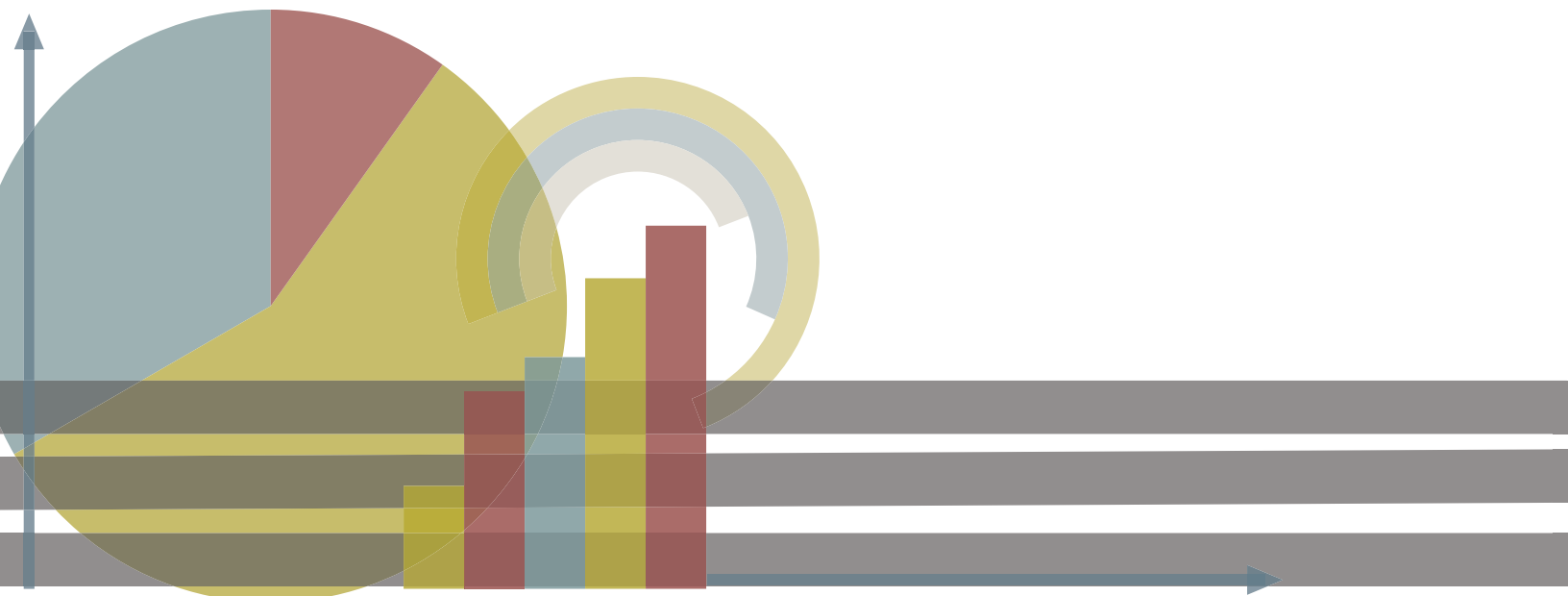
Pharmacists are more likely to think in terms of health conditions and medications than in terms of assets and sales. But independent community pharmacies today are also in the retail business and need to think like retailers. Considering income statements and balance sheets just as much as health care and outcomes can make or break your business.

“It’s important for pharmacy owners to understand the numbers side of the business so they can gauge whether or not they’re succeeding,” said Clark Balcom, Senior Vice President and Chief Operating Officer of PBA Health, a pharmacy services organization that provides business products and services for independent community pharmacies. “They—like all businesses—need to recognize trends and learn when to make changes in their operations and strategies. Only by regularly looking at the numbers are they able to do that.”

The market is tough for pharmacies. “Pharmacy is such a restricted business today with respect to how they get paid,” Balcom said. “They have to learn how to operate on thin margins. Successful independent pharmacies will do that by being enterprising—they’ll be looking to grow and expand their businesses.”

Tracking and measuring meaningful metrics about your business can give you the insight you need into your pharmacy’s performance. Whether you’re communicating with bankers, suppliers, prospective buyers or employees, these metrics provide an answer to an all-important question: How healthy is your business?

Get ready to dive into your numbers. Clark Balcom, pharmacy business expert, explains the top categories of metrics pharmacies should pay attention to, how to calculate them and what to do to improve your numbers.





SALES VOLUME & GROWTH

Businesses have to expand and grow in order to succeed. "When you think about growing sales, there are only so many ways you can do that," Balcom said. "Start looking into adding clinical services in conjunction with prescription growth. It's also important to let key employees know that growth is always an expectation."

Total Prescriptions

In independent community pharmacies today, 90 percent of sales are from prescriptions, so growing prescription sales is a must. This metric indicates the total number of prescriptions filled by the pharmacy and successfully picked up by the patient. This number showcases whether the business's volume is expanding or contracting.

Want this number to:



Total Return-to-Stock Prescriptions

This number reflects the total number of prescriptions filled by the pharmacy but never picked up by the patient. It means lost sales. "More important than the lost sale, however, is the potential clinical problem," Balcom said. "This number can be an early indicator of a potential disruption in a patient's proper use of medication or adherence." And, you have Star Ratings to consider. "Within certain therapeutic categories, the Centers for Medicare & Medicaid Services (CMS) will consider a disruption in refills a negative in terms of how you get measured by plans, so now reimbursement and network participation can be increasingly at risk," he said.

Want this number to:



How to improve: Filling prescriptions not picked up by patients is wasting resources. Look into improving total prescription rates, enhancing patient compliance and clinical programs, and improving inventory control.

Average Prescriptions per Day

For a more detailed look at total prescriptions, calculate average prescriptions per day.

How to calculate:

$$\frac{\text{Total Prescriptions (for a month)}}{\text{Number of Business Days (in that month)}}$$

Want this number to:



Average Return-to-Stock Prescriptions per Day

For a more detailed look at total return-to-stock prescriptions, calculate average return-to-stock prescriptions per day.

How to calculate:

$$\frac{\text{Total Return-to-Stock Prescriptions (for a month)}}{\text{Number of Business Days (in that month)}}$$

Want this number to:



Total Sales

This figure is the sum of total revenues, including reimbursements, co-pays and other store sales.

Want this number to:



Total Lost Return-to-Stock Sales

This number reflects the total unrealized revenues attributed to filled prescriptions that patients didn't pick up.

Want this number to:



Average Sales per Day

Every month, look at your pharmacy's average sales per day.

How to calculate:

$$\frac{\text{Total Sales (for a month)}}{\text{Number of Business Days (in that month)}}$$

Want this number to:



Average Lost Return-to-Stock Sales per Day

Every month, look at your pharmacy's average lost return-to-stock sales per day.

How to calculate:

$$\frac{\text{Total Lost Return-to-Stock Sales (for a month)}}{\text{Number of Business Days (in that month)}}$$

Want this number to:



Marketing & Sales Expense (as a percentage of sales)

This metric is a key performance indicator and goes beyond tracking sales or profits. It looks at what you're doing to cause sales to happen in the first place.

This number should be: No less than 3% of sales

How to improve: Growing and expanding your business will only happen through investing in marketing. "You need to have someone out there calling on doctors and marketing programs and services to the public," Balcom said. "You have to have someone looking at market demographics and identifying things like, 'Should I be in diabetics?' Somebody has to carry that flag and owners have to make the investment." Your competitors, namely national chain pharmacies, are investing huge dollars in marketing; you need to participate, too.

Prescriptions & Sales per Top Prescribers

Keep track of the total number of prescriptions and sales coming from each prescriber. **“Successful pharmacy owners (and their employees) know the prescriber relationships that drive their businesses, and they work diligently to build and preserve those relationships,”** Balcom said.

Prescriptions & Sales per Top Patient

It's important to know the total number of prescriptions and sales coming from each patient. "You have to know who your best patients are," Balcom said, "and work carefully to build trust, provide great care and go the extra mile to ensure that those patients are highly satisfied with your services."

PROFITABILITY

Profitability translates to your earning power. For example, do you have enough earning power to get a loan, or for someone to be interested in buying your business? Keep in mind that profitability doesn't mean cash flow. "You can end up with something that generates a lot of margin, but if it doesn't convert to cash in a proper timeframe, you can still go belly up," Balcom said. "When you look at profitability, start at the very top of the business and simply look at how you're doing overall," he said. Use the following metrics.

Gross Profit Margin (dollars)

This metric indicates what's leftover from sales to cover fixed costs, other operating expenses, interest and taxes. In pharmacy, it's primarily all of your sales minus what it costs to buy the inventory to support those sales.

How to calculate:

$$\text{Total Sales} - \text{Total Cost of Goods}$$

Gross Profit Margin Rate (percentage)

This metric reflects the percentage of every \$1 in sales that's available to cover fixed costs, other operating expenses, interest and taxes. For example, if a pharmacy has a gross profit margin rate of 25.74 percent, then \$0.2574 of every \$1 in sales is available to cover these costs.

How to calculate:

$$\frac{\text{Gross Profit Margin}}{\text{Total Sales}}$$

This number should be: More than 25% for retail pharmacy

Inventory Cost of Goods (as a percentage of sales)

This metric reflects the percentage of every \$1 in sales that's consumed by inventory expense. For example, if a pharmacy's inventory cost of goods as a percentage of sales is 74.26 percent, then \$0.7426 of every \$1 of sales is consumed by inventory expense. This is the reciprocal view of gross profit margin rate.

How to calculate:

$$\frac{\text{Total Inventory Cost of Goods}}{\text{Total Sales}}$$

This number should be: Less than 75% for retail pharmacy

Average Fee per Prescription Category

This metric looks at the average fee per prescription in a given category, such as all prescriptions, brand only, generic only, over-the-counter only, cash only, all third party prescriptions or by individual insurance plan.

"Ultimately, the numbers need to tell you if you can afford to be in that business," Balcom said. "That's never an easy decision for pharmacies. They don't want to lose any patients, but if your average fee per prescription for a certain insurance plan is significantly negative, then it's possible that you can't afford to be in that business."

How to calculate:

$$\frac{\text{Total Sales (in a given category)}}{\text{Total Number of Prescriptions (in a given category)}}$$

How to improve: Look beyond your storefront, and think and act strategically. "There comes a point where the business itself can't do all of the things necessary for the business to succeed," Balcom said. It's important to look beyond the local level and see what you can do more broadly. "If they're seeing reimbursements consistently go down year over year, maybe they need to stop and think, 'Why is that happening?,' 'What's empowering the PBMs to do that?,' 'How do I become a part of something bigger to change that part of my industry?' They have to question relationships that exist in the industry and consider what they can do to help turn that tide."

Average Inventory Cost per Prescription Category

When reviewed in combination with the average fee per prescription, this metric can give you insight into factors that affect your margin performance. For example, pharmacies can probe a decrease in margin and determine if it's due to a declining trend in category price, or to an inflationary trend in category supplier pricing (or both).

How to calculate:

$$\frac{\text{Total Inventory Cost (in a given category)}}{\text{Total Number of Prescriptions (in a given category)}}$$

PRODUCTIVITY & OPERATING EFFICIENCY

As a retail business, you need to operate at maximum efficiency. "Pharmacies have to know what hours of the day it makes sense to have certain staffing levels," Balcom said. "They have to know what days of the week they should be open—and when. And, they have to pay attention to the numbers in order to see those things." Make sure to closely watch important expense categories for pharmacies, such as payroll, general operating expenses and rent. Here's how.

Payroll Expenses per Employee

“Pharmacies have to hold the line on operating expenses, and the biggest one is payroll,” Balcom said. This metric represents the average payroll expense per employee.

How to calculate:

$$\frac{\text{Total Payroll \& Personnel Expenses}}{\text{Number of Full-Time Equivalent Employees}}$$

Sales per Payroll Dollar Expended

This metric represents the total dollars in sales generated for every dollar expended for payroll and personnel expense.

How to calculate:

$$\frac{\text{Total Sales}}{\text{Total Payroll \& Personnel Expense}}$$

Payroll Expense (as a percentage of sales)

“Payroll is huge, and paying close attention to payroll with respect to sales is a big part of efficiency,” Balcom said. This metric represents how much of every dollar in sales is consumed by payroll and personnel expense.

How to calculate:

$$\frac{\text{Total Payroll \& Personnel Expense}}{\text{Total Sales}}$$

Gross Margin per Payroll Dollar Expended

This metric represents the total dollars of gross margin the pharmacy generates for every dollar expended for payroll and personnel expense.

How to calculate:

$$\frac{\text{Gross Profit Margin (dollars)}}{\text{Total Payroll \& Personnel Expense}}$$

Total Operating Expenses (as a percentage of sales)

This metric represents how much of every dollar in sales is consumed by operating expenses.

How to calculate:

$$\frac{\text{Total Operating Expenses}}{\text{Total Sales}}$$

Sales per Pharmacy Square Foot

This metric represents the total dollars in sales generated for each square foot of “facility asset” used to support sales.

How to calculate:

$$\frac{\text{Total Sales}}{\text{Total Square Footage}}$$

Rent Expense per Square Foot

“Rent is always a significant expense in pharmacy that owners have to pay close attention to,” Balcom said. This metric represents annual rent on a per square foot basis.

How to calculate:

$$\frac{\text{Total Rent}}{\text{Total Square Footage}}$$

Rent Expense (as a percentage of sales)

This metric represents how much of every dollar in sales is consumed by rent expense.

How to calculate:

$$\frac{\text{Total Rent}}{\text{Total Sales}}$$

CASH FLOW, WORKING CAPITAL & ASSET MANAGEMENT EFFICIENCY

Managing your pharmacy's cash flow efficiently means having plenty of cash on hand to pay your bills, employees and suppliers. “Cash is king to every business,” Balcom said. You need to make sure you don't have cash tied up unnecessarily, and you need to align your receivables cycle with your payables cycle. “When you sell something, you want to collect cash faster than you have to pay your suppliers,” he said. Paying attention to the following metrics can help.

Aged & Past Due Accounts Receivable

Pharmacies need to make sure they're collecting cash for credit sales and paid claims as soon as possible. A regular review of aged receivables, and especially past-due receivables, is a must. Pay attention to the number of days it takes before a receivable actually gets converted to cash.

Accounts Receivable Turnover

This metric reflects the average number of times accounts receivable turns per year. A healthy pharmacy will always turn accounts receivable measurably faster than accounts payable.

How to calculate:

Total Annualized Portion of Sales
Coming from Credit Sales or Insurance
Claims (from the income statement)

Total Accounts Receivable (from the balance sheet)

Example: If 90 percent of the pharmacy's sales come from insurance and in-house charge accounts, then this number would be calculated as:

Total Sales x 0.90

Total Accounts Receivable

This number should be: More than 18

Accounts Receivable Turn Days

This metric captures how many days it takes, on average, for credit sales and insurance claims to convert to cash.

How to calculate:

365 (number of days in a year)

Accounts Receivable Turnover

This number should be: Less than 20 days

Total Inventory

It comes straight from the balance sheet and requires no calculation, but it's still important to keep a close eye on it. 🧴 When you see a bottle of inventory, pretend you're looking at a stack of cash because that's what it is: cash sitting on a shelf, 💰 Balcom said.

Total Inventory (as a percentage of sales)

This number is the same as Inventory Cost of Goods (as a percentage of sales) under Profitability, except you look at it from the perspective of cash flow and working capital efficiency.

Inventory Turnover

This metric reflects the average number of times a pharmacy turns its inventory in a given year.

How to calculate:

Annualized Inventory Cost of Goods
(from the income statement)

Total Inventory (from the balance sheet)

This number should be: More than 10

Inventory Turn Days

This metric captures how many days it takes, on average, to turn the pharmacy's inventory. Another way to look at it is, how many days of on-hand inventory is the pharmacy keeping on the shelf?

How to calculate:

365 (number of days in a year)

Inventory Turnover

This number should be: Less than 37 days

Accounts Payable Turnover

This metric reflects the average number of times accounts payable turns per year. A healthy pharmacy will always turn accounts payable slower than accounts receivable.

How to calculate:

Annualized Inventory Cost of Goods
(from the income statement)

Total Accounts Payable (from the balance sheet)

This number should be: Less than your Accounts Receivable Turnover



Accounts Payable Turn Days

This metric captures the average number of days the pharmacy is taking to pay suppliers. Pharmacies need to make sure they collect cash (or convert credit sales to cash) faster than they pay their suppliers. This is called aligning the pharmacy's accounts receivable and accounts payable cycles.

How to calculate:

365 (number of days in a year)

Accounts Payable Turnover

This number should be: More than your Accounts Receivable Turn Days

Sales to Assets (Asset Turnover)

Pharmacies have assets—buildings, computers, counters, shelves—to produce sales. If you're buying assets that don't support sales, then you're already violating a golden rule of business. This metric represents how many sales dollars the pharmacy is generating for every dollar that's invested in assets.

How to calculate:

Annualized Total Sales (from the income statement)

Total Assets (from the balance sheet)

How to improve: Always pay attention to how well your assets support sales, and to how well those assets support profitability or returns on those sales.

💡 Asset efficiency is a very important measure because if you're not doing a good job, it probably means you're buying a bunch of wasted assets. You need to stop doing that and get rid of those you already have, 🗑️ Balcom said.

Return on Assets

This metric represents how many operating profit dollars the pharmacy is generating for every dollar invested in assets.

How to calculate:

Operating Profit
(earnings before interest and taxes from the
income statement)

Total Assets (from the balance sheet)

SOLVENCY, STABILITY & LIQUIDITY

These measures determine your pharmacy's "staying power." Creditors look at the following metrics to see if your pharmacy has the right balance between debt and equity. They check to see if you have sufficient assets to cover all of your liabilities; if you have earnings in excess of the interest you owe on debt; and how your assets are paid. For example, are your assets paid out of the equity of the business or are they financed with debt? "Pharmacies need to look at their assets and liabilities and the operating performance of the business each year to determine if it's a stable business," Balcom said. "They should also be looking at monthly and annual trends to make sure things are heading in the right direction."

Current Ratio

This metric reflects how many dollars of current assets the pharmacy has to pay for each dollar of current liabilities.

How to calculate:

Current Assets

Current Liabilities

This number should be: More than 2

Quick Ratio

This metric reflects how many times the pharmacy can immediately cover its current liabilities if it had to.

How to calculate:

Cash + Accounts Receivable

Current Liabilities

This number should be: More than 2

Debt to Equity (*Net Worth*) Ratio

This metric reflects what is commonly referred to as “bankers’ or creditors’ risk.”

How to calculate:

$$\frac{\text{Total Liabilities}}{\text{Total Net Equity}}$$

This number should be: Less than 2

Debt Ratio

This metric reflects the percentage of pharmacy assets that are financed by debt.

How to calculate:

$$\frac{\text{Total Liabilities}}{\text{Total Assets}}$$

This number should be: Less than 50%

Equity Ratio

This metric reflects the percentage of pharmacy assets that are financed by equity.

How to calculate:

$$\frac{\text{Total Equity}}{\text{Total Assets}}$$

This number should be: More than 50%

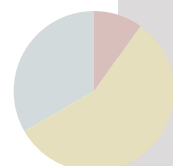
Times Interest Earned

This metric reflects how many times the pharmacy’s annual earnings exceed the interest payments the pharmacy owes.

How to calculate:

$$\frac{\begin{array}{l} \text{Operating Profit} \\ \text{(earnings before interest and taxes from} \\ \text{the income statement)} \end{array}}{\begin{array}{l} \text{Annualized Interest Expense} \\ \text{(from the income statement)} \end{array}}$$

This number should be: More than 7



As you measure your pharmacy's metrics, keep in mind that numbers are limited unless you use them to improve your business. "They're historical by nature," Balcom said. "They tell you what has happened, not what's going to happen. You have to take them and do something."

Tracking the right numbers consistently and responding to them will set you up for creating a more successful business. And it's not as hard as you might think.

TRACKING 101

When it comes to tracking your metrics, spreadsheet software is a pharmacy's best friend. Use these tips to make the most of your spreadsheets.

- *Color-code your metrics.* Use the standard color-coding of red to designate "bad" and black to designate "good."
- *Update regularly.* Track your metrics on a monthly basis. That way, you can look quarter-to-quarter, semester-to-semester and year-to-year. It may also be helpful to compare a month, quarter or semester to the same period in the previous year.
- *Use charts and graphs.* Visual representations can make recognizing upward and downward trends easier.
- *Include benchmarks.* Incorporate up-to-date industry benchmarks next to each metric, so you can see if you're performing better or worse compared to other pharmacies. (You can easily find benchmark data in the annual NPCA Digest from the National Community Pharmacists Association.)

WHAT'S NEXT?

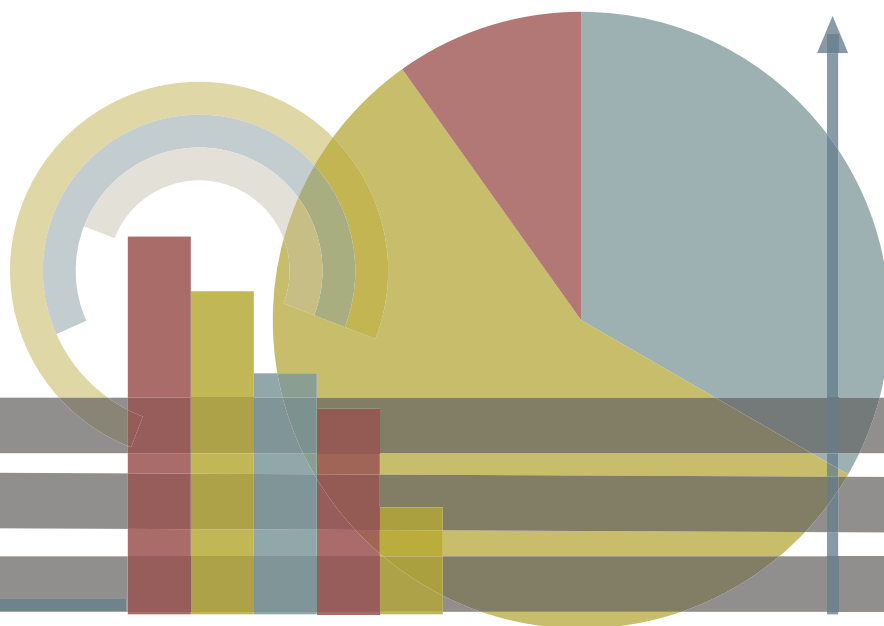
If you're interested in improving your metrics—and learning to better respond to them—take a look at ProfitGuard, a service from PBA Health that can help you manage your business better. Learn more at pbahealth.com/profitguard.



ABOUT THE EXPERT

Clark Balcom is the Senior Vice President and Chief Operating Officer of PBA Health, a pharmacy services organization dedicated to independent community pharmacies. Balcom is committed to advancing the role of community pharmacy in the

delivery of convenient, affordable and essential health services. He is a financial, business and technology integration expert. He began his career with Accenture and spent many years aligning strategies, people, processes and technology in the delivery of multiple industry and corporate solutions for Fortune 500 companies. Since joining PBA Health in 1996, Balcom has been a leader in the development of the company's principal products and services. He remains active in the daily innovation and delivery of solutions that help independent community pharmacies succeed.



Your Business Profile

Fill in this worksheet to get an overview of the health of your pharmacy business.

SALES VOLUME & GROWTH

Total Prescriptions _____

Total Return-to-Stock Prescriptions _____

Average Prescriptions per Day _____

Average Return-to-Stock Prescriptions per Day _____

Total Sales \$ _____

Total Lost Return-to-Stock Sales \$ _____

Average Sales per Day \$ _____

Average Lost Return-to-Stock Sales per Day \$ _____

Marketing & Sales Expense _____ % of sales

Prescriptions per Top Prescriber _____

Sales per Top Prescriber \$ _____

Prescriptions per Top Patient _____

Sales per Top Patient \$ _____

PROFITABILITY

Gross Profit Margin \$ _____

Gross Profit Margin Rate _____ %

Inventory Cost of Goods _____ % of sales

Average Fee per Prescription Category \$ _____

Average Inventory Cost per Prescription Category \$ _____

PRODUCTIVITY & OPERATING EFFICIENCY

Payroll Expenses per Employee \$ _____

Sales per Dollar Expended \$ _____

Payroll Expense _____ % of sales

Gross Margin per Payroll Dollar Expended \$ _____

Total Operating Expenses _____ % of sales

Sales per Pharmacy Square Foot \$ _____

Rent Expense per Square Foot \$ _____

Rent Expense _____ % of sales

CASH FLOW, WORKING CAPITAL & ASSET MANAGEMENT EFFICIENCY

Aged & Past Due Accounts Receivable \$ _____

Accounts Receivable Turnover _____

Accounts Receivable Turn Days _____ days

Total Inventory \$ _____

Total Inventory _____ % of sales

Inventory Turnover _____

Inventory Turn Days _____ days

Accounts Payable Turnover _____

Accounts Payable Turn Days _____ days

Sales to Assets (Asset Turnover) \$ _____

Return on Assets \$ _____

SOLVENCY, STABILITY & LIQUIDITY

Current Ratio _____

Quick Ratio _____

Debt to Equity (Net Worth) Ratio _____ %

Debt Ratio _____ %

Equity Ratio _____ %

Times Interest Earned _____

FIND OUT HOW TO IMPROVE YOUR PHARMACY'S NUMBERS.

Email this completed form to info@pbahealth.com or fax to 816-245-5702. Information is confidential.