

Royal Pharmacy and Home Health Ltd.

Timothy P. Stratton
Ben Wu

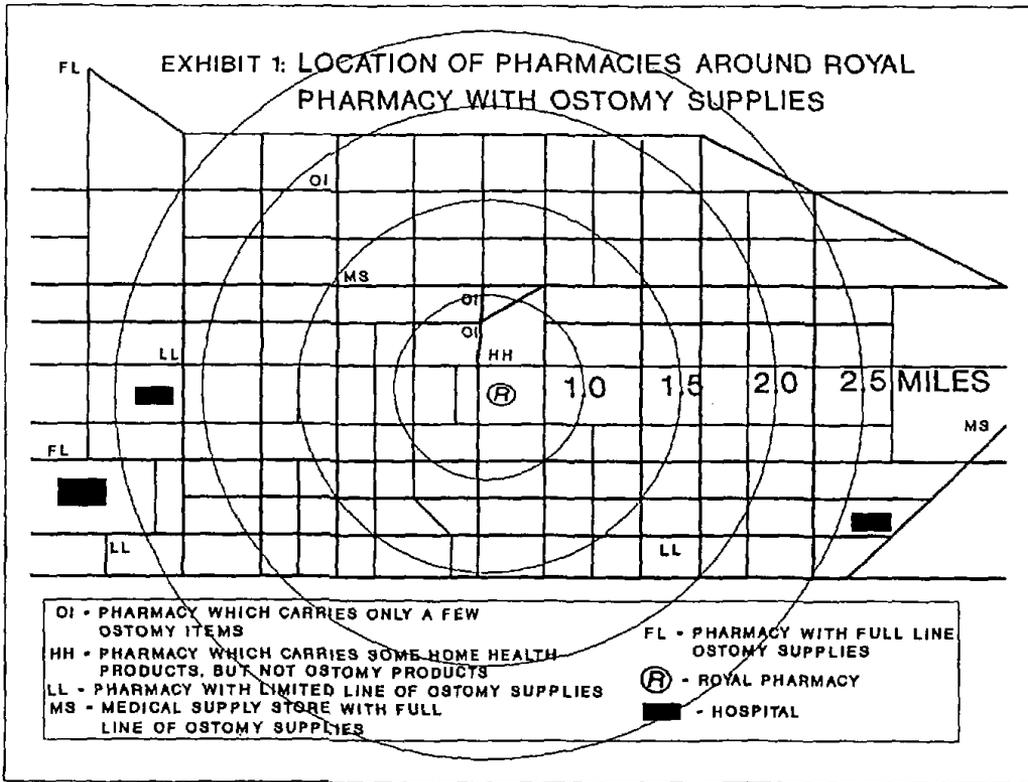
PROBLEM

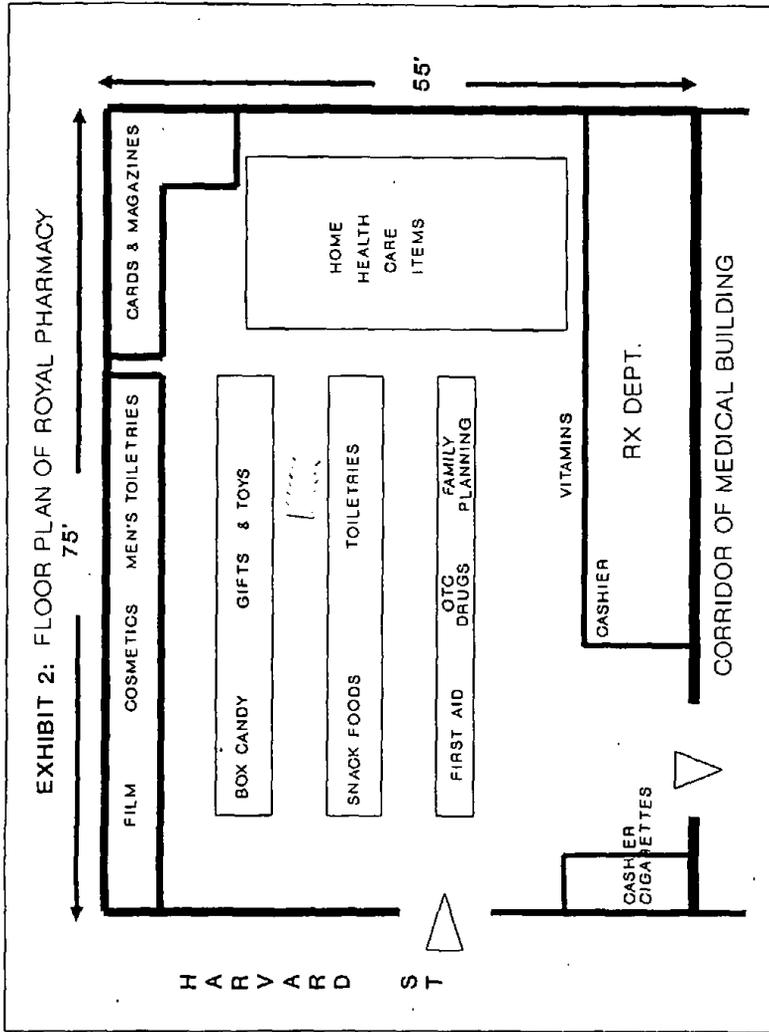
Jason Lim, the pharmacist-owner of Royal Pharmacy, was sitting in his office swallowing an aspirin. Jason had been worrying about his home health business since the pharmacy down the street, Gilbert's Pharmacy, had added a home health section two months ago. Jason believed that he had lost some of his home health patients to Gilbert's Pharmacy.

Jason's Royal Pharmacy is located in a medical building in a middle-income residential area of Vancouver, British Columbia. Royal Pharmacy has been serving this neighborhood for ten years, while Jason has been the owner for the last three years. Pharmacy competition is fierce, with 17 pharmacies located within a 1.5-mile radius of Jason's pharmacy. These competitors include independent and chain pharmacies, several of which carry home health care items (Exhibit 1). Since Royal Pharmacy is located in an area with several medical buildings, it does not surprise Jason that he has encountered so many competitors.

To gain an advantage over his competitors, Jason added a home health section to his pharmacy 18 months ago (Exhibit 2). Since then, Jason has been promoting Royal Pharmacy as a home health

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care center. Revenue from the home health section has been improving steadily over the year.

Royal Pharmacy is a certified distributor of home health care products for a major home health care product manufacturer. With this distributorship, Royal Pharmacy receives special discounted prices for the company's home health care products. In exchange, Royal Pharmacy has agreed to carry a full line of the company's products, as well as to counsel all the patients purchasing the company's products. Home health care products carried by Royal Pharmacy include bathtub rails, elevated toilet seats, walkers, crutches, quadcanes, wheelchairs, shower seats, canes, hospital beds, and bedpans.

Royal Pharmacy also carries an extensive line of compression anti-embolism stockings. The manufacturers of these stockings require store staff to be trained in fitting the stockings. In addition to home health items, Royal Pharmacy carries a variety of consumer-oriented products such as cigarettes, candies, magazines, toiletries, first-aid supplies, film, and popular nonprescription drugs (Exhibit 2).

Jason has recently revised the staffing schedule for Royal Pharmacy (Exhibit 3). He has decided that it would be more appropriate for him to dedicate more time to managing the pharmacy, so he will be spending less time in the dispensary than he has been.

Royal Pharmacy is open Monday through Friday from 9:00 a.m. until 7:00 p.m. and on Saturday and Sunday from 10:00 a.m. until 5:00 p.m. Jason has been charging a professional fee of \$6.20 per prescription for the last 3 months (up from \$5.85), still well below the \$7.06 per prescription permitted under the government agreement.

As Jason entered the dispensary and leaned against the dispensary counter wondering what he might do about his pharmacy operation, the phone rang. "Good morning, Royal Pharmacy. Can I help you?" Jason answered in an emotionless tone.

"Good morning. My husband had a colostomy done recently. Your ad in the *Yellow Pages* says that you carry home health care products. I would like to order a few ostomy items for my husband," said the elderly sounding woman.

"Oh, I'm sorry. We don't carry ostomy supplies," Jason replied apologetically.

EXHIBIT 3

Royal Pharmacy Staffing Pattern

Job Title	FTE ¹	Hours ²	Salary
Pharmacist	1.35	Pharmacist 1: Mon-Fri 10am-7pm Pharmacist 2: Sat-Sun 10am 5pm Owner covers 9am-10am, lunches and breaks on weekdays.	\$19.00/hr
Pharmacy Assistant	1.40	Assistant 1: Mon-Fri 10am-7pm Assistant 2: Mon&Fri 10am-7pm	\$ 6.10/hr
Cashier	1.15	Cashier 1: Mon-Thu 9am-6pm Cashier 2: Fri 9am-6pm Sat 10am-5pm	\$ 6.25/hr
General Clerk	1.83	Clerk 1: Mon-Fri 9am-6pm (Wed Off) Sun 10am-5pm Clerk 2: Mon-Fri 11am-7pm	\$ 6.00/hr
Cosmetics Clerk	0.95	Clerk 1: Tue-Fri 10am-7pm Sat 10am-5pm	\$ 6.10/hr
Delivery Person	0.47	Delivery 1: Mon-Fri 4pm-6pm Sat 4pm-6:30pm	\$ 5.50/hr
Owner	1.00	Mon-Fri 9am-6pm	\$21.00/hr

¹FTE=Full Time Equivalent, 40 hours per week.

²A one-hour lunch break included for all staff (except delivery).

“No! But your ad says that you sell home health products! I’ve tried six pharmacies in the neighborhood, and none of them carries ostomy supplies!” exclaimed the caller.

“Ma’am, where do you live?” Jason asked, trying to help.

“I live about three blocks east of your pharmacy, beside the supermarket,” answered the woman.

“I see,” said Jason. “You might try Medline Medical Supplies down on Woods Street. It’s about a 30-minute drive from your house.” Jason hung up the phone after the lady had thanked him.

This kind of inquiry was not new to Jason. When a doctor who was working in the medical building asked for Jason’s advice on

certain ostomy items last week, Jason realized that in recent months more and more people had been asking him questions about ostomy products. He decided to call a meeting with his two staff pharmacists to discuss the possibility of adding a line of ostomy products to his existing home health section. As the three pharmacists talked, the following questions were discussed: How many potential ostomy customers are there in our city? Who would be our major ostomy competitors? How much money would be needed to get this started? Many crucial questions remained unanswered. These questions prompted Jason to do some research.

Jason first checked a reference book to learn more about ostomies and ostomy care (Exhibit 4). He also contacted the United Ostomy Association, which provided him with some data relating to ostomy patients (Exhibits 5 and 6). He learned that the prices charged for ostomy supplies by his potential competitors were very close to the retail prices suggested by the manufacturers (usually a 33% markup on cost).

Census Tract information revealed that there were about 45,000 people living within 2.5 miles of Royal Pharmacy, and the *B.C. Directory* indicated that many residents within this area listed their occupations as "retired."

As part of his research, Jason arranged a meeting with the enterostomal therapist from a local hospital. From this meeting, Jason learned that most colostomy, ileostomy, continent ileostomy, and urostomy-ileal conduits were permanent. Colostomy, ileostomy, and urostomy were by far the most common types of ostomy. The length of time that temporary ostomates had their ostomies varied from two to six months, on average. The therapist estimated that there were about 6,000 ostomates living in B.C., 2,000 of them in the Vancouver area. The City of Vancouver alone gained about 360 new ostomy patients each year.

The enterostomal therapist always referred her patients to medical supply houses which carry full lines of ostomy supplies. Examples of ostomy supplies and accessories are given in Exhibit 7. Her referrals were based on the location, services, and product selection of the medical supply houses. Free delivery services, the therapist pointed out, were welcomed by many patients. To the therapist's

EXHIBIT 4

OSTOMY

"Ostomy" describes a surgically-induced opening into a body cavity or organ, or is the name given to the operation which is performed to create that opening. Ostomy surgery is performed when a gastrointestinal tract disease becomes life-threatening or difficult to control through non-surgical means. More than one million North Americans, from newborns to 90-year-olds, have ostomies. Hundreds of thousands of new ostomies are performed in Canada and the United States every year.

Types of Ostomies

The most common type of ostomy is the colostomy, followed by the ileostomy. The urostomy is the least common. Colostomies and urostomies are performed because of disease, trauma or a birth defect; ileostomies are performed primarily due to disease.

Enterostomal Therapists

Enterostomal therapists are nurses specifically educated in the care of individuals with stomas and draining wounds. Enterostomal therapists are the ostomate's most important counselling resource. Other health professionals who care for ostomates also rely on the enterostomal therapist for expert advice.

Products and Equipment

Ostomates can choose disposable (temporary) or reusable (permanent) pouches. Closed-ended pouches tend to be used when regulation is by natural methods or irrigation.

Reference: Yen M. Ostomy care. In: Canadian Pharmaceutical Association. Canadian self medication. Ottawa: Canadian Pharmaceutical Association, 1984: Ch. 28.

knowledge, there were no pharmacies or medical supply houses in the Greater Vancouver area that had an enterostomal therapist on staff. The therapist concluded the meeting by telling Jason that Pharmacare, the provincial pharmacy insurance program, was investigating the possible overuse of ostomy supplies in the province of British Columbia.

After three weeks of research, Jason believed that he had gathered sufficient information, including financial data on his store's operations, to make a decision (Exhibit 8). Should Royal Pharmacy enter the ostomy care business?

EXHIBIT 5

United Ostomy Association
of North America Data (1989)

Total Members: 44,236 (2,793 are non-ostomates)

Membership Breakdown by Age
(15,575 members reporting)

Age	Members	Percentage
0-18	238	1.5
19-29	370	2.4
30-39	1116	7.2
40-49	1839	11.8
50-59	2972	19.1
60 +	9040	58.0

Membership Breakdown by
Type of Ostomy
(19,491 members reporting)

Ostomy Type	Members	Percentage
Permanent colostomy	9287	47.6
Temporary colostomy	116	0.6
Ileostomy	6661	34.2
Continent ileostomy	222	1.1
Urostomy	2560	12.9
Colostomy and urostomy	293	1.5
Ileostomy and urostomy	155	0.8
Urostomy-ileal conduit	Nil	Nil
Reconnected ostomy	125	0.6
Unknown type	126	0.7

SOLUTION

The marketing problem in this case involves positioning. Pharmacies, like other firms, products or services, will be categorized by consumers according to attributes important to those consumers, such as selection, personalized service, and price. To attract a particular group of consumers (i.e., a particular market segment), a pharmacy must develop and implement a marketing strategy that

EXHIBIT 6

United Ostomy Association
of Vancouver, B.C. Data (1989)

Total Members: 372 (25 are non-ostomates)

Membership Breakdown by Age
(347 members reporting)

Age	Members	Percentage
0-18	7	2.0
19-29	15	4.3
30-39	24	6.9
40-49	40	11.5
50-59	51	14.7
60 +	210	60.5

Membership Breakdown by
Type of Ostomy
(347 members reporting)

Ostomy Type	Members	Percentage
Permanent colostomy	149	42.9
Temporary colostomy	Nil	Nil
Ileostomy	136	39.2
Continent ileostomy	13	3.7
Colostomy and urostomy	Nil	Nil
Ileostomy and urostomy	2	0.6
Urostomy-ileal conduit	47	13.5
Reconnected ostomy	Nil	Nil

sets it apart; i.e., differentiates it from other pharmacies in the minds of the consumers it wishes to reach (1).

Royal Pharmacy is a small, well-established independent pharmacy in a downtown neighborhood. The concentration of medical buildings nearby is both advantageous and detrimental to Royal Pharmacy. While these medical practices generate a large volume of prescriptions, the high number of physicians in the area has attracted an almost unbelievable amount of pharmacy competition. In response to the phenomenal competition, Jason has developed a marketing niche for Royal Pharmacy, positioning his store against his competitors as a home health care center. The success of this

EXHIBIT 7
OSTOMY CARE PRODUCTS

- ADHESIVE REMOVER
- ANTIFUNGAL
- ANTISEPTIC
- DEODORANT
- INCONTINENCE GARMENT
- OSTOMY CARE
- SKIN BARRIER
- SKIN PROTECTANT
- URINARY ANTISEPTIC
- URINARY DRAINAGE

Reference: Canadian Pharmaceutical Association. Canadian self medication. Ottawa: Canadian Pharmaceutical Association, 1984.

strategy is evidenced by the increasing sales from that department over the past year (Exhibit 8). Unfortunately, a nearby competitor has also now entered the home health care market, threatening Jason's position.

To prevent erosion of his market, or even to increase his level of

EXHIBIT 8

ROYAL PHARMACY AND HOME HEALTH, LTD.

BALANCE SHEET

	1989	1990
CURRENT ASSETS		
Cash	\$ 61,804	\$ 13,450
Accounts receivable	\$ 98,405	\$110,166
Prescription inventory	\$239,428	\$292,128
OTC inventory	\$110,942	\$114,639
Home health inventory	\$106,110	\$101,942
Cosmetics inventory	\$ 95,209	\$100,834
Other inventory	\$125,417	\$143,161
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TOTAL CURRENT ASSETS	\$837,315	\$876,320
Fixtures and equipment	\$ 62,865	\$ 55,322
Less accumulated depreciation	\$ 7,543	\$ 6,639
NET FIXTURES AND EQUIPMENT	\$ 55,322	\$ 48,683
Prepaid expenses	\$ 9,382	\$ 10,435
	-----	-----
TOTAL ASSETS	\$902,019	\$935,438
	=====	=====
CURRENT LIABILITIES		
Accounts payable	\$598,283	\$617,431
Notes payable < 1 year	\$ 5,000	\$ 0
Accrued expenses	\$ 6,730	\$ 5,493
	-----	-----
TOTAL CURRENT LIABILITIES	\$610,013	\$622,924
Notes payable > 1 year	\$ 50,000	\$ 45,229
	-----	-----
TOTAL LIABILITIES	\$660,013	\$668,153
OWNER'S EQUITY (NET WORTH)	\$242,006	\$267,285
	-----	-----
TOTAL LIABILITIES + NET WORTH	\$902,019	\$935,438
	=====	=====
SALES		
Prescription Sales	\$ 472,984	\$ 469,500
OTC Sales	\$ 315,153	\$ 313,450
Home Health Sales	\$ 128,967	\$ 286,972
Cosmetic Sales	\$ 94,789	\$ 94,003
Other Sales	\$ 96,002	\$ 95,672
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TOTAL SALES	\$1,107,895	\$1,259,597

EXHIBIT 8 (CONTINUED)

ROYAL PHARMACY AND HOME HEALTH, LTD.

INCOME STATEMENT

	1989	1990
COST OF GOODS SOLD		
Prescription drugs	\$ 354,727	\$ 361,515
OTC medications	\$ 226,814	\$ 225,684
Home Health Equipment	\$ 86,408	\$ 192,271
Cosmetics	\$ 47,394	\$ 51,702
Other goods	\$ 76,802	\$ 75,864
	-----	-----
TOTAL COST OF GOODS SOLD	\$ 792,145	\$ 907,036
GROSS MARGIN	\$ 315,750	\$ 352,561
EXPENSES		
Owner Salary	\$ 43,000	\$ 43,680
Employee Wages	\$ 135,974	\$ 170,014
Rent	\$ 23,976	\$ 24,576
Heat, light, power	\$ 2,523	\$ 2,474
Accounting and legal fees	\$ 4,887	\$ 5,610
Taxes and licenses	\$ 4,897	\$ 5,096
Insurance	\$ 3,472	\$ 3,472
Interest paid	\$ 6,821	\$ 6,344
Repairs	\$ 2,046	\$ 3,879
Delivery	\$ 2,208	\$ 2,915
Advertising	\$ 9,000	\$ 10,000
Bad debts	\$ 957	\$ 763
Telephone	\$ 2,876	\$ 2,954
Miscellaneous	\$ 31,674	\$ 29,355
TOTAL EXPENSES	\$ 274,401	\$ 311,132
NET INCOME BEFORE TAXES	\$ 41,349	\$ 41,429
Interest Income	\$ 520	\$ 942
	-----	-----
TOTAL INCOME (before tax)	\$ 41,869	\$ 42,371
	=====	=====
CASH IN		
Cash at beginning of year	\$ 7,639	\$ 68,648
Cash and bank card sales	\$ 382,421	\$ 380,260
Payment on accounts receivable	\$ 598,734	\$ 614,166
Withdrawals from personal savings	\$ 0	\$ 0
Long-term bank loan	\$ 50,000	\$ 0
	-----	-----
TOTAL CASH IN	\$1,038,794	\$1,063,074

EXHIBIT 8 (CONTINUED)

ROYAL PHARMACY AND HOME HEALTH, LTD.

STATEMENT OF CASH FLOW

	1989	1990
CASH OUT		
Owner salary	\$ 43,000	\$ 43,680
Employee wages	\$ 135,974	\$ 170,014
Rent	\$ 23,976	\$ 24,576
Heat, light, power	\$ 2,523	\$ 2,474
Accounting and legal fees	\$ 4,887	\$ 5,610
Taxes and licenses	\$ 4,987	\$ 5,096
Insurance	\$ 3,472	\$ 3,472
Interest paid	\$ 6,821	\$ 6,344
Repairs	\$ 2,046	\$ 3,879
Delivery	\$ 2,208	\$ 2,915
Advertising	\$ 9,000	\$ 10,000
Bad debts	\$ 957	\$ 763
Telephone	\$ 2,876	\$ 2,954
Miscellaneous	\$ 31,674	\$ 29,355
Payments on accounts payable	\$ 702,589	\$ 738,492
	-----	-----
TOTAL CASH OUT	\$ 976,990	\$1,049,624
NET CASH FLOW	\$ 61,804	\$ 13,450
	=====	=====

sales, Jason has four options, as suggested by the Product/Market Expansion Grid (2). Based upon this model (Exhibit 9), Jason can further differentiate himself from his competitors by pursuing new products, new markets, or both. Jason is considering diversification, introducing a new product line (ostomy supplies) to a new market (ostomy patients). His hope is that diversification will further differentiate Royal Pharmacy from his competitor who recently entered the home health care market.

Ostomy Market Potential

British Columbia has one of the fastest-growing elderly populations in Canada, and Exhibit 5 shows that approximately 60% of all ostomates are over 60 years of age (3). Additional epidemiologic trends reveal that the incidence of Crohn's disease, and therefore the number of ostomates, has been rising over the past two decades (4). As one-third of all current ostomates in British Columbia live in Vancouver, the growth potential for the ostomy market in the Vancouver area appears to be very strong indeed.

EXHIBIT 9

PRODUCT/MARKET EXPANSION GRID

	Existing products	New products
Existing markets	1. Market penetration	3. Product development
New markets	2. Market development	4. Diversification

Reference: Ansoff HI. Strategies for diversification. Harvard Bus Rev 1957;35(Sept-Oct):113-24.

Other Market Considerations

Although the ostomy market appears to have excellent growth potential, many other factors must be considered in determining whether or not Royal Pharmacy should become involved in the ostomy care business. The business environment, existing and future competition, price, and attributes unique to the ostomy market must all be examined.

As health care expenditures increase, the government continues to seek ways to control these costs. The enterostomal therapist in the case indicated that Pharmacare, the provincial pharmacy insurance plan, was undertaking an investigation of possible overuse of ostomy supplies, which are covered by Pharmacare. Because Pharmacare is the largest payer for ostomy care devices in the province, a decision to restrict reimbursement for these supplies could have an adverse impact on the growth potential of this market (5). Jason must pay particular attention to developments in this area and should be in close contact with Pharmacare officials as the investigation proceeds.

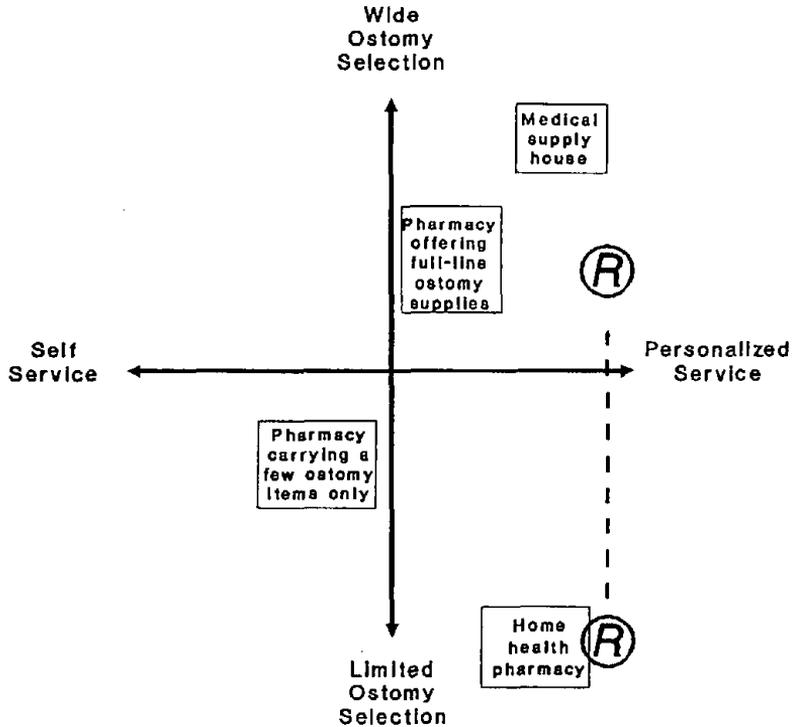
A market niche exists only as long as competition does not enter that niche (6). Jason must analyze his proposed ostomy supply market in terms of competitor location, competitor product and service offerings, and competitor pricing policies. Exhibit 1 shows that only 3 pharmacies within Royal Pharmacy's 1.5-mile neighborhood trading area carry any ostomy supplies whatsoever. A medical supply house is also located within this radius, however, carrying a full line of ostomy supplies. Additional competitors emerge as the trading radius is expanded to the 4.5-mile range considered necessary to support a home health care business (4). The population density of Vancouver is very high, with 45,000 people living within 2.5 miles of Jason's pharmacy; therefore, by not having to expand his trading area as much as recommended, Jason will probably be able to de-emphasize some of his more remote potential competitors.

To differentiate himself from other pharmacies offering ostomy supplies, Jason can offer better selection and/or more complete services, such as delivery and extensive patient counseling, as suggested by the enterostomal therapist. Such a strategy will be necessary to achieve market penetration, drawing existing customers away from other sources, as well as attracting new ostomates (Exhibit 10) (7). Differentiating himself in this way from the beginning will also enable Jason to solidify his position in the market, affording at least some protection against market erosion should a competing pharmacy presently offering a limited number of ostomy supplies decide to expand its ostomy line.

Offering greater selection probably cannot be used to differentiate Royal Pharmacy from the medical supply houses because of the medical supply houses' greater sizes and inventories. Instead, Jason can differentiate himself from these competitors by promoting patient convenience. While Royal Pharmacy can meet both the medication and ostomy supply needs of patients in one location, medical supply houses are prohibited from dispensing drugs.

Pricing of the ostomy products is one market variable that Jason will probably not want to manipulate, as most ostomy supply retailers currently charge approximately the same price; moreover, the 25% gross margin on ostomy supplies is already lower than the margin for many other items in the pharmacy. Choosing not to alter prices will not obviate the need for Jason to shop the competition

EXHIBIT 10
IMAGE POSITIONING MAP
FOR ROYAL PHARMACY
AMONG OSTOMY PATIENTS



(R) = Royal Pharmacy. Dotted line shows the movement that is hoped for after introducing a full-line, full-service ostomy department in the pharmacy.

periodically, however, to ensure that his pricing policies remain competitive (8).

The initial decision to rent or purchase home health equipment or supplies, including ostomy care products, usually results from a referral made to the patient by a health care professional (4). Thus,

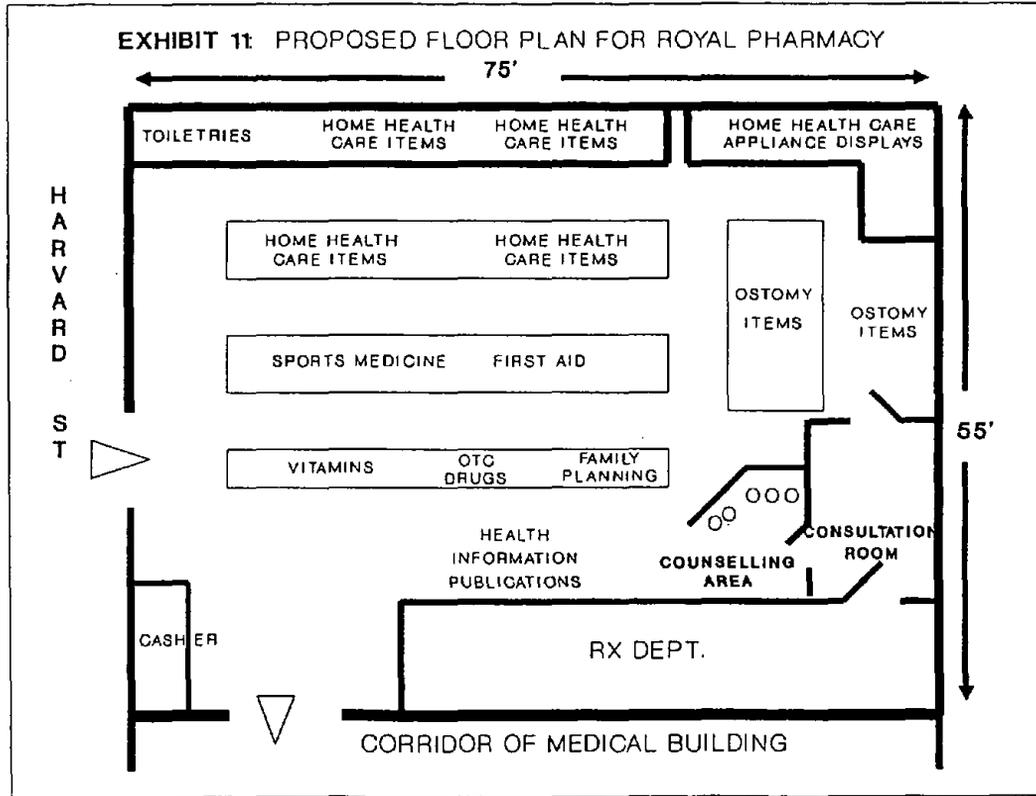
Royal Pharmacy must promote its home health center not only to patients, but to health care professionals as well. Furthermore, health care providers such as enterostomal nurses often order home health care products from community pharmacies for hospital use, thus making these health care professionals direct consumers as well as potential referral sources.

Assessing Current Pharmacy Operations

Many nonmarket considerations must also be taken into account when deciding whether or not to pursue a new market, such as the capability of the firm to provide the service it promotes (7). In assessing Jason's existing store operations, several points are worthy of note. Jason's attempt to create a home health care center image for Royal Pharmacy is incomplete at best. While carrying and promoting home health care supplies, he continues to offer products for sale—tobacco, gifts, and toys—that directly contradict the professional health care image he desires. These items constitute only a small percentage of his total sales (Exhibit 8). Elimination of this merchandise would not only solidify Royal Pharmacy's health care image, but would also improve the stagnant inventory situation and free up valuable floor space for additional home health care merchandise, such as ostomy supplies.

Jason should consider altering the layout of Royal Pharmacy, constructing a consultation room to provide for confidential counseling of home health and ostomy patients (Exhibit 11). In addition to providing privacy, such a room would further enhance that professional pharmacy image that Jason is trying to achieve. It is estimated that construction of a private counseling area would cost \$5,000 (Canadian), with an additional \$800 for furnishings and installation of a telephone line.

The case indicates that Jason's staff receives excellent product training from the manufacturers of home health care supplies. Royal Pharmacy has several staff training options. Jason and his entire staff could receive training through manufacturers' programs. While training clerks would enable these staff members to provide more complete customer service, there is frequently a high turnover rate among clerks, adding to training costs as new clerks are



brought on line. Clerks will also lack the training necessary to address the other health needs of patients, and referring patients to clerks for ostomy counseling may dilute the professional image of the pharmacists. Training pharmacists in ostomy care will enable them to provide more complete service to their patients, but will also require pharmacist time for training and patient counseling. Finally, Jason should be certain that he receives training in ostomy care, as this will enable him to assist his staff pharmacists when they are occupied with other duties. Proper training in this area will also enable Jason to make the right decisions regarding ostomy inventory. This training, of course, is going to require time on Jason's part, and he may have to stagger work schedules to minimize disruption of his pharmacy's operations during the training periods.

Ostomy patients have unique psychological needs related to their medical conditions which must be met, and pharmacy staff are not likely to receive the training necessary to meet these needs (5). Royal Pharmacy has the option of hiring an enterostomal therapist, a person highly trained to handle all of the emotional as well as the physical aspects of the ostomy patient. As most ostomy care business arises from referrals by physicians, hospital nurses, and hospital-based enterostomal therapists, a pharmacy-based enterostomal therapist would be in a better position to promote the pharmacy's ostomy care department to other health care professionals and ostomy patient support groups. Hiring an enterostomal therapist would provide Royal Pharmacy with an immediate advantage over all competitors because no other ostomy supply retailer in Vancouver has an enterostomal therapist on staff. The major drawback to hiring an enterostomal therapist is the high salary commanded by the therapist (salaries are similar to those of staff pharmacists).

Royal Pharmacy should hire an enterostomal therapist part-time at first. This would provide the advantages of having the enterostomal therapist while minimizing the costs. At the same time, Jason and his staff pharmacists should receive training in ostomy care from the therapist, as well as from the manufacturers' representatives. This would enable the pharmacists to assist patients more fully when the therapist was unavailable. In-depth patient counseling with the therapist could be arranged on an appointment basis, and Jason or one of his pharmacists should assist the therapist in as

many counseling sessions as possible. This will not only increase the pharmacists' capabilities in this area, but also will help to position the pharmacist as a true member of the health care team in the minds of patients. Because of the competitive nature of the ostomy business in Jason's trading area, ostomy consultations should be provided at a nominal fee or free of charge until Jason is established in the ostomy market (7).

Financial Analysis

To carry a full line of ostomy care products would require an inventory in excess of \$20,000. Located in a major city, Royal Pharmacy can receive a product usually on the same day it is ordered. For this reason, inventory might be reduced to \$15,000 without compromising product selection. Inventory should be geared toward colostomy and ileostomy patients, as these two categories represent the largest percentage of ostomates (Exhibit 6). The ostomy center should also be well stocked in ostomy accessories such as karaya powder, clips, examination gloves (latex and vinyl), deodorizers, ostomy belts, and finger cots. Accessories should comprise 10% of the ostomy inventory, about \$1,500. Thus, the minimum inventory investment becomes \$16,500.

From Exhibit 12 it is estimated that \$22,780 will be required to set up the ostomy care center. It is assumed that the ostomy product manufacturers offer a 12-hour seminar, spread over 2 weekdays. It is further assumed that these seminars are offered free to pharmacy employees. An additional \$13,770 will be required to pay for the center's fixed annual operating expenses. Royal Pharmacy's financial statements reveal that the store has \$13,450 in cash available. A portion of this amount (\$2,780) could be contributed toward development of the ostomy care center, with the balance of the start-up costs being covered with a \$20,000 bank loan at an interest rate of 13% (\$2,600 per year). The remaining cash balance could be kept in reserve to cover operating expenses in the first few months of operation, when the ostomy department's business would be expected to be slow until patients learn of the center's existence.

For variable costs, it is assumed that products will be priced at 33% above cost. If each ostomy patient purchases \$100 worth of

EXHIBIT 12

ESTIMATED OSTOMY CARE CENTER EXPENSES

<u>Initial Setup Expenses</u>		<u>Fixed Operating Costs</u>	
Inventory	\$16,500	Phone line	\$ 600
Construction	\$ 5,000	Therapist ³	\$ 9,120
Furnishings	\$ 600	salary ³	
Phone line	\$ 200	Promotion	\$ 1,200
Staffing costs		Subscription	\$ 250
Owner ¹	\$ 252	to ostomy	
Pharmacist ²	\$ 228	care journal	
		Loan interest	\$ 2,600
	-----		-----
Total	\$22,780	Total	\$13,770

¹ \$21.00/hour X 12 hours.

² \$19.00/hour X 12 hours.

³ \$19.00/hour X 10 hours/week X 40 weeks/year.

supplies each month from the pharmacy, the cost of goods sold becomes \$75 per patient per month.

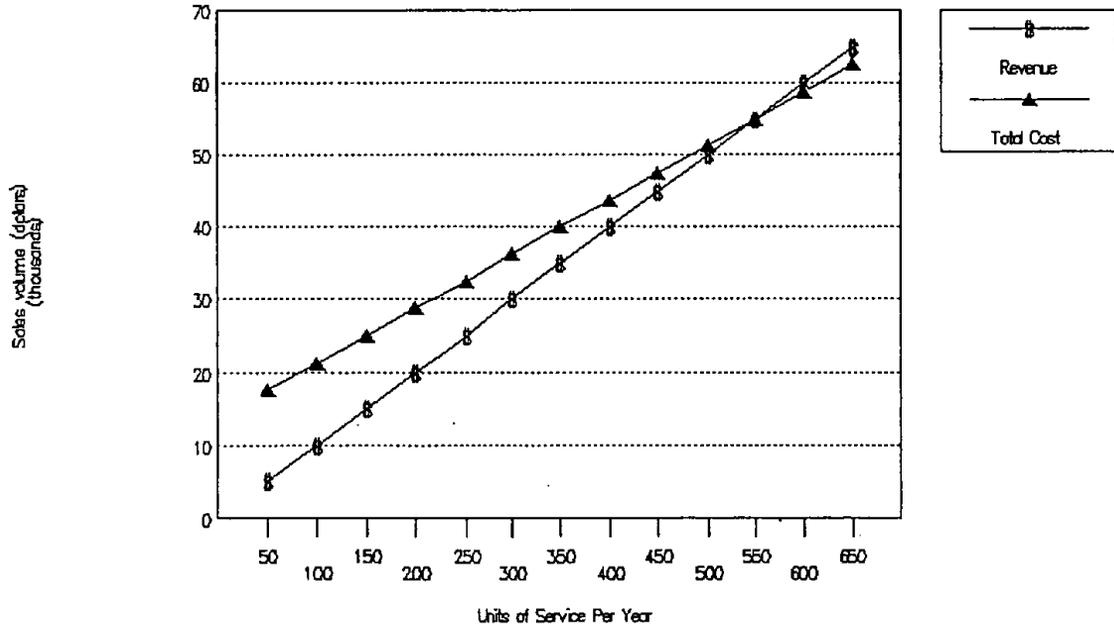
Break-even analysis (Exhibit 13) reveals that the new ostomy care center would require 46 patients purchasing \$100 worth of ostomy supplies each month. Since approximately 2,000 ostomy patients live in Vancouver, Royal Pharmacy must capture only 2.3% of the market to break even. If the pharmacy can capture as little as 4% of the market (80 patients per month), the ostomy supply department should generate a profit of \$10,050 in the first year alone, enabling the \$20,000 bank loan to be paid off in a little over 2 years. The break-even analysis suggests that the establishment of an ostomy care center at Royal Pharmacy is financially feasible.

CONCLUSION

Royal Pharmacy should secure a \$20,000 bank loan, construct a patient counseling area, and develop an ostomy care center. Jason and his staff pharmacists should receive training in ostomy care, and Jason should hire a part-time enterostomal therapist. Such a center would permit Royal Pharmacy to quickly differentiate itself from the stiff competition in its trading area. The growth potential

EXHIBIT 13

Ostomy Center Break-Even Analysis



for the ostomy market, the favorable break-even analysis, and Royal Pharmacy's existing presence in the home health care area suggest that such a venture should be very successful.

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