Association of Independent Multiple Pharmacies

**MEMO: KEY RISKS ARISING FROM A DOMINANT MAIL ORDER PHARMACY PROVIDER**

## 1. Introduction:

THE SUNDAY TIMES | Today's sections | Past six days | Explore | Times Radio | Log in | Subscribe | Search

# Amazon's next high street target: your local chemist

Sabah Meddings

Sunday March 14 2021, 12.01am, The Sunday Times

Amazon's prescription service may face hurdles in the UK, where pricing is regulated
REUTERS

## 2. Executive Summary

2.1. This paper sets out the key risks for patients, the NHS and community pharmacy from the emergence of a dominant distance selling mail order pharmacy provider, such as Amazon.

2.2. Community Pharmacy provides excellent value for the taxpayer for two fundamental reasons:

i. There is a fixed Community Pharmacy Contractual Framework (CPCF) envelope for income, with costs being borne in full by contractors

ii. Contractors compete on service to maximise their access to the CPCF envelope and remain financially viable, and therefore must provide an excellent service to patients in order to survive.

2.3. There are two fundamental risks to the sustainability of the network:

i. Insufficient quantum of funding within the CPCF. If, overall, the income provided by the CPCF cannot cover the basic cost base of pharmacy, then business failure is an inevitable outcome.

ii. Inadequate distribution of CPCF funding between pharmacy contracts*. This is not to say that CPCF funding should be shared equally between pharmacy contracts, as that would not incentivise good service, but that if a certain few mail order pharmacy contracts have access to significantly disproportionate share of the CPCF, then the remaining CPCF funding available is too small to sustain the rest of the network.

**Note the difference between a pharmacy contract (individual site locations) and a pharmacy contractor (pharmacy businesses ranging in scale from independents to national multiples, which can have multiple contracts). In this instance, the former is the relevant point of interest.*

2.4. Existing mail order pharmacies are not particularly innovative or profitable – they simply exist due to financial doping by their owners who fund substantial losses. Quite simply, the cost of mail is too expensive to offset the standard dispensing fee and cost of customer acquisition, yet mail order pharmacy persists due to the pervading global tech "logic" of loss-making titans.

2.5. The community pharmacy industry is **sleep-walking** towards mail order proliferation, the negative impacts of which will be significant. A better outcome would be for policy-makers to ensure that the community pharmacy ecosystem continues to ensure long-term access and sustainability, by taking the necessary steps to avoid mail order dominance.

Association of Independent Multiple Pharmacies

## 3. Resilience and strength of service provided by existing community pharmacy network

3.1. Community Pharmacy has been recognised for its resilience and accessibility during the pandemic, and is generally rated highly in terms of service outcomes vs expectation compared to other areas of primary care.

3.2. But **why** does CP have such high resilience and service? The answer is as follows:

- Rather than an underlying human characteristic of pharmacy professionals relative to their counterparts elsewhere in the NHS, the fundamental difference relates to ecosystem and incentives, as explained below:

3.3. The key outcome of our contractual framework is that **Community Pharmacies compete on service**

3.4. This is the case because all of the following apply simultaneously:

3.4.1. They are private businesses where the owner personally encounters the risks and rewards of their endeavours. Poor service is punished financially as patients go elsewhere, and pharmacy businesses decline, with their owners' facing capital loss. Conversely, good service is rewarded through positive financial outcomes as income is largely linked to activity.

3.4.2. Switching costs for the patient are low (Compare for example how easy it is to change pharmacy vs changing GP), and therefore there is very little lock-in to an individual contract and a high degree of choice for the patient.

3.4.3. At 10,000+ community pharmacies nationally, there is plenty of alternative choice (this is a strength of the network not a weakness)

3.4.4. Community Pharmacies are largely remunerated on individual units of activity as they are performed (e.g. numbers of items, numbers of NMS performed etc), and therefore every interaction counts financially.

3.4.5. Unlike other countries (e.g. Ireland) there is no price competition on prescriptions, so the only remaining competitive dynamic is service. This is why community pharmacy businesses strive to compete with each other on:

- Relocating to most convenient site for patient attraction
- Opening hours
- Speed and friendliness of service
- Ensuring minimum staffing levels
- Product availability

- Providing value added services for free (e.g. Dossette box dispensing, home delivery, ATM-style collection, click & collect, app-ordering)

3.5. As we can see, from a government perspective, the outcomes created by the community pharmacy model are exceptionally valuable.

3.6. Conversely, the GP model can be described as:

- Largely per-capita funded with low choice and high switching cost (ie. difficult to change surgery easily).
- Therefore, the service level offered has a substantially lower direct impact on the financial outcome for the practice owner

.

3.7. In summary, when compared with a GP practice, the pharmacy has to pick up the phone because it cannot afford not to, and hence a better level of service is provided. (The same goes for opening the pharmacy in bad weather, dealing with operational problems etc).

## 4. The Funding Envelope

4.1. The above section describes the excellent deal that the UK taxpayer is getting on pharmacy, with pharmacies falling over each other to provide first-rate service.

4.2. In addition, given that there is a fixed envelope, the cost of providing this excellent service is borne entirely by the contractors and not the NHS.

4.3. This paper focuses on the disruption to the marketplace caused by the potential dominance of mail order pharmacy providers, and therefore does not discuss in detail the size of the envelope itself.

4.4. However, it is self-evident from the plight of community pharmacies as highlighted by EY in their paper entitled “Impacts of current funding, policy and economic environment on independent pharmacy in England” (Sep 2020), that the quantum of funding contained in the CPCF is insufficient.

Association of Independent Multiple Pharmacies

## 5. Why does the emergence of mail-order dominance threaten the viability of community pharmacy?

5.1. The proliferation of mail order pharmacies threatens the viability of community pharmacy due to two overarching factors:

1. Financial pressure on bricks and mortar community pharmacies
2. The internet naturally creates dominant business models

5.2. **Financial pressure on bricks and mortar community pharmacies arises from the following factors:**

**5.2.1. Squeezing of the envelope:**

5.2.1.1. There are approximately 11,400 community pharmacy contracts in England that share the £2,592m income from provided under the CPCF.

5.2.1.2. The average contract therefore receives income of around £230,000, and the distribution of income between bricks and mortar pharmacies is relatively flat, compared to when the top 3 distance selling pharmacies are included.

5.2.1.3. The following data sets show relevant statistics for Nov 2020:

**Overall market**:

| | |
|---|---|
| Number of contracts: | 11,427 |
| Number of items: | 83,579,037 |
| Mean average items in month: | 7,314 |
| Median average items: | 6,479 |

**Data for largest 3 mail order pharmacies:**

| Rank | Contractor | Nov 2020 items | Items market share | Multiple of items vs median contractor |
|---|---|---|---|---|
| 1 | Pharmacy2U | 549,171 | 1.28% | 84.8x |
| 2 | Echo | 333,796 | 0.70% | 51.5x |
| 3 | Well.co.uk | 69,323 | 0.15% | 10.7x |

**Data for largest 3 bricks and mortar pharmacies**:

| Rank | Contractor | Nov 2020 items | Items market share | Multiple of items vs median contractor |
|---|---|---|---|---|
| 1 | West Elloe Pharmacy, Spalding Lincolnshire | 46,134 | 0.06% | 7.1x |
| 2 | Woodlands Pharmacy, (Washington, Tyne & Wear) | 37,313 | 0.05% | 5.8x |
| 3 | Woodhouse Pharmacy, Sheffield | 35,905 | 0.04% | 5.5x |

5.2.1.4. It is clear from the above, that if a very small number of contracts access a relatively large share of the CPCF envelope, then accordingly the remaining envelope is spread much thinner across the remaining bricks and mortar pharmacies. This will have a similar impact of a funding cut, ultimately risking the viability of bricks and mortar pharmacies.

### 5.2.2. Skimming the market

5.2.2.1. There is a skewing effect due to the nature of mail order patients relative to the patients likely to continue to use bricks and mortar pharmacies for their prescription needs.

5.2.2.2. Distance selling pharmacies will likely over-index on:

- Stable repeat patients with simpler medication requirements and low co-morbidity
- Original pack patients

5.2.2.3. Conversely, Bricks and mortar pharmacies will like over-index on:

- MDS patients
- Controlled drugs and supervised consumption
- Cold chain drugs
- Complex patients / high co-morbidity

5.2.2.4. Therefore, in addition to the effect of reducing the available CPCF available for community pharmacy, there is a secondary effect that the relative cost of service / income ratio increases as “easy-to-serve” patients are skimmed into the mail order sector.

### 5.2.3. Operational gearing

5.2.3.1. Community pharmacies have high fixed costs (namely rent, rates, utilities, staffing). Therefore, even a small reduction in patients attending community pharmacies will directly impact the net profit of the pharmacy as these fixed costs cannot be reduced accordingly. Given that Community Pharmacies are already showing low profit margins, the funding envelope squeeze will likely put many pharmacies into loss.

5.2.3.2. In other words, the often-quoted idea that "there will always be many people will never go online and would prefer to use their community pharmacy for prescriptions", does not prevent the failure of the network.

**5.2.4. Uncontrolled vs controlled impact**

5.2.4.1. The impact of the well-publicised 2016 funding cut which has ultimately led to the current challenging situation for pharmacy may well be dwarfed by impact of mail order dominance:

5.2.4.2. Under the 2016 funding cut, the CPCF envelope was cut by 7.4% from £2,800m to £2,592m

5.2.4.3. Comparatively, online market shares of disrupted industries tends to be much larger, as shown:

- Retail: 26% (2020 UK Data: Centre for Retail Research)
- Grocery: 30% (2020 UK Data: Statista)

*Note that mathematically, the percentage growth in market share of the mail order sector is by definition the percentage decline in CPCF available to Bricks and Mortar

5.2.4.4. Furthermore, the size of the impact is uncontrolled. In the government funding cut, the cut was specifically 7.4%. However, in the mail order case, the reduction in CPCF available to the bricks and mortar sector is not limited by agreement with DHSC/NHSE or not is the pace and sale predictable.

5.3. **Why does the internet create dominant players?**

5.3.1. Dominance on the internet is a clearly evident outcome, with most disrupted industries having often only up to 3 leading players, and often less. Can you easily name the other significant players in each of the example industries below?

| Industry | Largest players |
|---|---|
| Retail | Amazon |
| Internet search | Google * |
| Teleconferencing | Zoom*, Microsoft Teams |

| | |
|---|---|
| Taxi ride hailing | Uber* |
| Streaming | Netflix*, Amazon Prime, Disney+ |
| Food delivery | Just Eat, Uber, Deliveroo |

5.3.2. * Dominance in industry can be so acute that some companies have become verbs in their own right – something that very few companies in history have achieved.

5.3.3. The above companies preside in markets with limited significant competition because they have created high barriers to entry:

**5.3.3.1. The requirement to fund sustained losses**

5.3.3.1.1. Typically, the online disruption model has played out as follows:

- Drive revenue whilst ignoring costs and therefore incur deep losses
- Increase market share to reduce competition
- Convince the funding market (venture capital or stock market analysts) that the business, despite its deep losses, has immense value because it will eventually do one of the following:
  - Become the monopoly provider once it has put existing players out of business
  - Sell itself to a larger disruptive company (usually a tech giant)
  - Find a new way of monetising the data generated by users

5.3.3.1.2. Most businesses cannot sustain losses, and those that do can only do so because of two funding sources:

- Ultra High risk investors (for example Softbank in the case of WeWork and Uber).
- Funding from other group companies (for example Amazon's highly profitable cloud services arm (Amazon Web Services) bank rolling its retail business which has made large losses for many years.

5.3.3.1.3. This model is already playing out in pharmacy, where the largest player, Pharmacy2U has failed to make a profit in any year since it's founding in 1999, but has continually sourced venture capital funding.

5.3.3.1.4. The Pharmacy2U model is not in any way innovative – it simply is one of the few businesses that can afford to offer free home delivery by post to all customers as it does not need to make profit to survive. Community Pharmacy has always offered free home delivery, although has not typically promoted it to every single patient for fear of making losses

5.3.3.2. **Internet marketing dynamics**

5.3.3.2.1. Given that most internet journeys start with a google search, and there can be by definition only a single top-listed link for a particular search term, dominance typically goes to the players who score highest early on google, and then this reinforces. The first page of google search results has been reported to capture 90%+ of all post-search clicks. Therefore, it is difficult to maintain varied competition amongst internet-based providers

**5.3.3.3. Mail order businesses are locationally independent**

5.3.3.3.1. Given that the actual location of a mail order provider is irrelevant, the industry need not have multiple providers.

## 6. Impact on society

6.1. Dominance of mail order pharmacy will have a far reaching impact on society beyond the devastating impact to bricks and mortar contractors.

### 6.1.1. Reduced access for care:

6.1.1.1. The above factors demonstrate that financial distress for bricks and mortar pharmacy is an inevitable consequence of a significant diversion of CPCF funding share flowing to mail order pharmacy. The consequences of distress, most notably inevitable closures and reduced access to pharmacy provision, are the same as those identified in the EY (Sep 2020) report "Impacts of current funding, policy and economic environment on independent pharmacy in England", and therefore are not covered in full detail here.

6.1.1.2. The distress caused will likely lead to reduced community pharmacy access for those that have requirements that cannot be easily achieved through remote means or mail order:

- Complex patients including those that require MDS, Controlled Drugs, Refrigerated lines
- Services particularly those that can only be delivered in person such as flu/COVID vaccines, supervised methadone consumption
- Immediate prescription dispensing for acute conditions
- Immediate advice and OTC purchases
- Patients who have limited access to the internet
- Patients who have limited access to a convenient mailbox that can be accessed securely and in a short-timeframe, and thus cannot accept mail order.

6.1.1.3. The corollary of the above is, inevitably, more pressure on the GP and A&E system, as patients with such needs are unable to access their local community pharmacy

6.1.1.4. It is worth noting the rural and small-town community pharmacies, rather than those clustered in metropolitan areas, may well have a higher risk of diversion, and therefore, closure as these are already less likely to be within walking distance of people's homes, and a higher proportion of homes in these areas can receive parcels to safe places more easily (ie. less people living in apartments)

### 6.1.2. Resilience, health economics, governmental and other risks

6.1.2.1. Resilience, as displayed by the robust medicines supply during the pandemic despite extreme demand shocks, is cited as a key strength of community

pharmacy. This resilience arises from having multiple sites of access to back each other up, combined with the last point of care being close to the patient's home, which results in localised and tailored problem solving. Comparatively, a mail-order driven model carries high resilience risk due to the following reasons:

- The impact of operational failure (fire, flood, cyber attack, virus outbreak etc) is much larger
- Delivery network failure (e.g. overload of mail services), as no walk-in option is available
- Problems cannot be creatively solved locally
- It is not as straightforward to take your prescription to another provider

6.1.2.2. The current ecosystem works (perhaps too) well for Government and the taxpayer, with significant bargaining power enjoyed by DHSC/NHSE with a lack of dominance from a single pharmacy contract. Under a scenario of a high proportion of prescriptions dispensed by a single player such as Amazon, the bargaining power moves back the other way, as alternative models of care would likely have been eliminated from the market.

6.1.2.3. In addition to the above, there is clearly a political view that the NHS is "not for sale" and certainly "not for sale in America". Is there really an appetite from the taxpayer for a US tech giant to be the key deliverer of the nation's medicine? Naturally a counter-argument would be that the two largest players (WBA & McKesson) are American owned, however it should be noted that:

- These businesses have significant UK heritage
- These companies pay significant UK tax and create large employment within the community
- Neither operator has dominance in the UK market.

6.1.2.4. The existing eco-system provides a significant tax revenue for the Exchequer, particularly through business rates, corporation tax and National Insurance. Comparatively, the government will have to weigh up the potential lost taxes through dominance by large tech firms in this sector.

6.1.2.5. Bricks and mortar pharmacies employ significant numbers of people in every community in the country. Comparatively, in the dominant distance selling scenario, employment will be lower in number and concentrated in central "logistics-friendly locations" and away from rural, suburban and coastal areas.

6.1.2.6. Furthermore, rather than paying rent to UK-tax-paying landlords for their shopfronts, online businesses typically have to an alternative type of "rent" to Google and Facebook (also US tech giants) to maintain the online visibility.

6.1.2.7. As discussed, mail-order pharmacy has very challenged unit-economic model, with the existing per-item fee and retained drug margin (together approximately £2 per item) very low compared to the cost of last-mile delivery.

Inevitably, the business model that might attract big tech players to this market needs to involve other revenue sources namely:

- Utilisation of data (albeit with consent which will patients will be asked to provide to access the service) for link-selling purposes
- Selling of aggregated data to third parties
- Utilisation of data to drive advertising business models
- As a loss-leader to gain market share in an unrelated industry (for example, Amazon using pharmacy as a loss leader to increase Amazon Prime membership)

6.1.2.8. A significant shift to mail order pharmacy will have negative impacts on the environment arising from excessive use of packaging, and further use of home deliveries by vehicle when 89% of the population in England has access to a community pharmacy within a 20 minute walk (source: PSNC)

6.1.2.9. Policy-makers should consider what happens when a dominant online pharmacy business is sold to another provider with a different strategic direction that is not in the public interest (for example: tech companies, foreign government-associated organisations). In this instance, the sale could be considered a back-door entry into the NHS.

6.1.2.10. As noted earlier, thus far online pharmacy has proven to be a loss-making enterprise as the income from dispensing is insufficient to meet the cost of distribution and the cost of patient acquisition.

6.1.2.10.1. This invariably drives online players to employ increasingly confusing and aggressive marketing tactics to acquire customers cheaply, as the normal way of doing so (ie. paying for google adverts) becomes incredibly expensive. See below for examples:

**Figure 1**: Pharmacy2U acquiring a banner link under the listing page for family-owned "Bassett Pharmacy" (previously known as Sunak Pharmacy – run by the Chancellor's mother) on the Evening Standard online local directory. *This screenshot was taken on 15 March 2021*

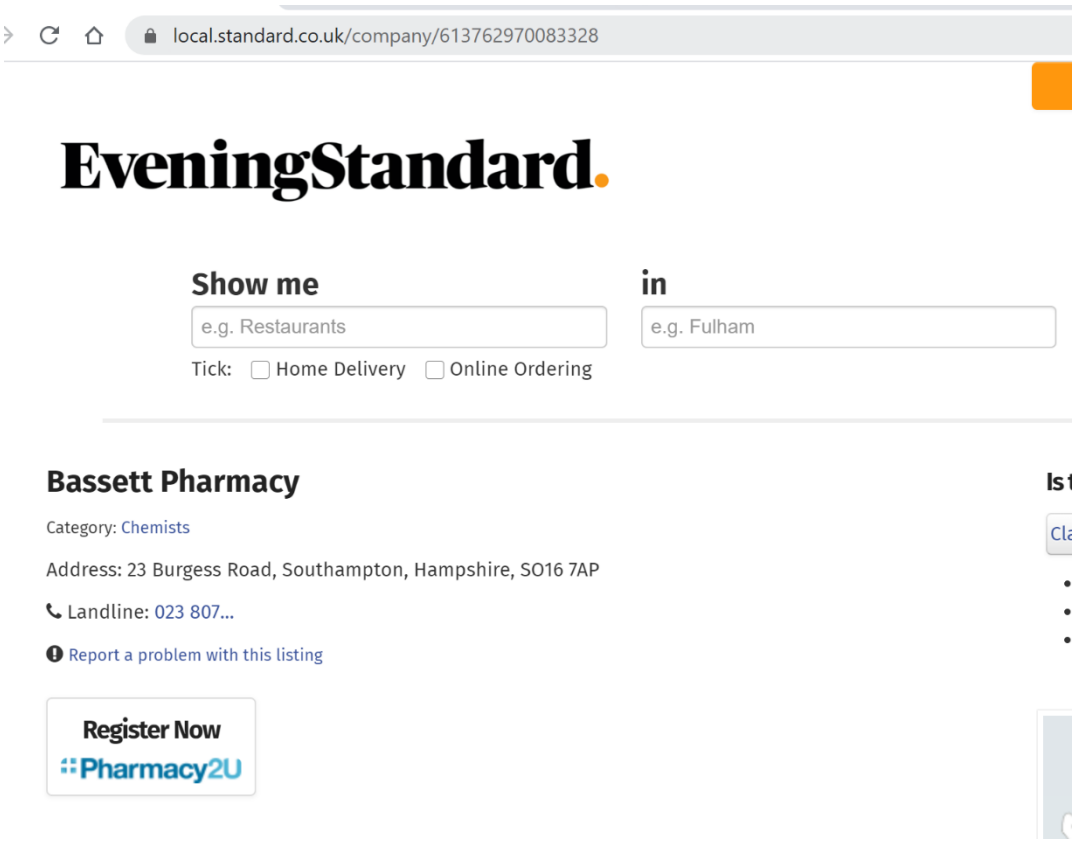


**Figure 2**: The Advertising Standards Authority upholding a complaint against Pharmacy2U in 2018.


https://www.asa.org.uk/rulings/pharmacy2u-ltd-a17-406348.html

**Figure 3**: C&D article regarding a marketing campaign by Echo Pharmacy.

# Lloyds pulls Echo marketing email after patient inducement 'concerns'

by **Grace Lewis** 12/03/2021 | 10 comments | News


AIMp: "Contractors (small and large)" rose concerns about the Echo email

**Lloydspharmacy has pulled a marketing email from its campaign following concerns that it incentivised patients to sign up to its Echo delivery service.**

Association of Independent Multiple Pharmacies

## 7. Is it all worth it?

7.1. In most cases, the "creative destruction" of innovation has vast benefit to society. For example, despite the toll on traditional retailers, the arrival of Amazon in the UK has undoubtedly improved outcomes for retail consumers in three areas:

7.1.1. **Price** – customers are able to compare multiple sellers instantly and choose the cheapest

7.1.2. **Selection** – Amazon offers a wider range of products than would be accessible locally on the high street

7.1.3. **Convenience** – Via next day Home delivery

7.2. Note that none of the above actually apply for pharmacy:

7.2.1. **Price** – the customer is not paying in this instance, as the cost of medication is reimbursed by NHS

7.2.2. **Selection** – Everyone in the country has access within their local community to every drug required on a same day basis.

7.2.3. **Convenience** – Every pharmacy offers home delivery and could offer it more widely if they were reimbursed to do so.

7.3. Considering the three factors above, it is important for policy makers to ask the question: Is it all worth it?

Association of Independent Multiple Pharmacies

## 8. So what next?:

8.1. It is clear that policymakers need to agree a way forward so as not to sleep-walk into an era of mail order dominance, potentially by Amazon, that would threaten the exceptionally high value model that already exists.

8.2. However, it is important to preserve the features of the pharmacy ecosystem that bring such exceptional value for money and service to the taxpayer compared to other areas of primary care.

8.3. The arguments presented in this paper are not necessarily obvious and need to be presented to ministers and Key Opinion Leaders in order to ensure their merits are understood.

8.4. A well-funded and organised media and PR campaign to "save the NHS from Amazon Pharmacy" in the UK should be coordinated proactively, including a national petition to gain groundswell. This will influence the discourse in a manner so as to sustain community pharmacy.

8.5. Potential policy routes to explore should include.

8.5.1. A funded delivery service available for local deliveries but not mail order

8.5.2. A limit to share of CPCF that can be accessed by mail order, for example:

- A maximum number of items that a single pharmacy contract could by reimbursed for
- A maximum funding available to the mail order sector as a whole

8.5.3. The revocation of pharmacy licences for businesses continually making significant losses to prevent financial doping (analogous to the Financial Fair Play rules in sport)

8.5.4. The requirement for a parliamentary debate prior to the granting of a pharmacy licence to an American tech giant.

8.5.5. A policy for NHSE to refuse to grant the provision of a contract to specific entrants such as Amazon on the grounds of public interest.

8.5.6. Strict rules on advertising online pharmacies. A ban on online pharmacy advertising could be considered, or regulatory action including revocation of licence against overly confusing or aggressive marketing.

8.5.7. Clear Provisions to prevent the sale of an mail order pharmacy business as a going concern or the customer list to be sold to a third party to prevent sudden new arrival of a pharmacy owner that is not in the public interest.

8.5.8. Reinforcement that the patients' nomination is with the pharmacy contract not with the pharmacy contractor. Therefore, any movement in nomination from one DSP to another (either within an existing group or pursuant to a sale of a DSP) is strictly prohibited without a new nomination by the patient, and for GPhC action to be taken in such circumstances.

8.5.9. Clear reinforcement by GPhC that distance selling pharmacies are not allowed to charge for deliveries either directly or indirectly. For example, free delivery cannot be linked or bundled into a loyalty, membership or subscription scheme such as Amazon Prime. (Note that Under the National Health Service 2006 (Part 1 1(3)), all NHS services must be provided free of charge except where a charge has been expressly mandated by legislation. As no legislation has been passed that would allow this, it would be against the Act to request payment for the delivery of a prescription. Bricks and mortar pharmacies are able to charge for delivery as part of a private service (except where the item is a Part IXA specified appliance))

8.5.10. A level playing field to be created by GPhC / MHRA in the areas of:

8.5.10.1. Temperature control – Currently the guidance for postal delivery by mail and wholesale transport are completely misaligned with the former requiring no temperature controlled transport but the latter being mandated by MHRA, despite potentially longer transportation times in the post.

8.5.10.2. Requirements for the education and training of pharmacy support staff – the new GPhC guidance effective from October 2020 clearly states minimum training requirements for pharmacy delivery drivers but no such mandate applies to the drivers employed by the postal and courier services

8.5.11. Consideration of a minimum level of pharmacists per X thousand nominated patients to ensure standards of care and advice are available.

8.6. This paper does not endorse the following routes of actions:

8.6.1. Abolition of volume-linked payment for prescriptions as this is the fundamental driver towards good service.

8.6.2. A two-tiered prescription dispensing fee, as this may later promote diversion directly towards mail order providers by NHS stakeholders (e.g. CCGs)

8.6.3. Abolition of a national CPCF in favour of local funding decisions on reimbursement prescription dispensing.