Coping with the structural change and financial pain from 1 August

'THE big questions,' says Bruce Annabel, 'are whether the generic manufacturers and, to a lesser extent, wholesalers will be able to maintain the traditional level of discount percentages once the Government's 12.5 per cent clawback kicks in, and to what level can pharmacy successfully increase generic substitution rates.'

Mr Annabel, partner in charge of pharmacy services at Johnston Rorke, believes the structural changes brought about by the 1 August commencement of the Federal Government's generic drug 12.5 per cent price reduction policy will inevitably bring a degree of financial pain for pharmacy even if suppliers maintain existing discount percentages.

Pharmacists will have already noticed the big changes coming to effect from 1 August in the PBS Yellow Book.

Among simvastatin products alone, it includes 26 new generic product presentations, with every brand and generic product receiving a 12.5 per cent cut in the 'price-to-pharmacy' benchmark, while two of the branded simvastatin products have taken a brand price premium (BPP).

A further 21 new generic products across 10 other therapeutic groups are also included, all of which have had the Government's 12.5 per cent 'clawback' applied. Added to these are more BPP products, increased therapeutic group premiums (TGP) and, for the first time, the special patient contribution (SPC) which is applied to products which receive a BPP.

As Mr Annabel says, these therapeutic groups represent very large PBS costs to the Federal Government and include the statins, which are biggest of all in both volume dollars and volume scripts. Also of note are the SSRIs, antihypertensives, analgesics (a small dollar but big script volume item) and antineoplastic agents (including some high price cancer drugs).

Mr Annabel explained to the *AJP* that with the 12.5 per cent 'clawback', he believed the Government aimed to:

- take back some of the generic product 'incentives' being enjoyed by generic manufacturers and retail pharmacies to reduce PBS growth;
- push some drugs out of the PBS net and completely into the customer's financial responsibilities by dropping the total selling value to or below the $28.60 general co-payment threshold;
- compel customers to pay more for certain drugs ('that is, if you want it you'll have to pay for more of it because we don't want to!');
- encourage customers to switch from branded drugs to generics via the increased BPP, new BPPs, increased TGPs and the SPC—all to reduce PBS costs; and
- force brand pharma, generic manufacturers, wholesalers and retail pharmacies to absorb some financial pain.

Mr Annabel says it's this last point where retail pharmacy profits could be significantly affected.

'The reason is that "brand pharma" sell and wholesalers distribute those branded products that the customer is being encouraged to switch away from in preference to the cheaper generic lines. Obviously that will impact their sales and prof-

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Financial impact of 12.5 per cent 'clawback'

BRUCE Annabel recently addressed the Community Pharmacy Southern Convention and Exhibition where he analysed of the potential financial impact of the Government's 12.5 per cent 'clawback'.

This analysis first assumed the generic incentive and wholesaler discount percentage would remain as is (30 per cent and 4.3 per cent respectively). Second, he analysed the outcome if the generic incentive dropped to 20 per cent and the wholesaler discount was removed.

In the first scenario, using a generic simvastatin 40mg as the example, retail pharmacy sale value would fall 11.7 per cent ($9.09) and gross profit dollars (GP$) would drop by 10.6 per cent ($3.31).

However, the result for a branded simvastatin would see the sale value fall 11.6 per cent ($9.09) and GP$ by 8.3 per cent ($1.19). Obviously the drop in the branded margin is much less because there is much less 'discount' to lose, although the generic item still produces more than double GP$.

The outcome here is that the Government saves $9.09, pharmacy loses $3.31 or $1.19, the generic manufacturer loses $5.78 and brand pharma/wholesaler combined lose $7.90. So the obvious question is who will absorb the $7.90? And how much of that will be passed on to retail pharmacy?

Under the second scenario, again using simvastatin 40mg, the generic sale value would fall by $9.09 (11.7 per cent), the same as the no change scenario, while GP$ would drop by $9.09 (29.2 per cent)!

In the brand case the sale would fall by the same while GP$ would go down by $3.70 (25.9 per cent). Again the GP$ generated by the generic are still more than double the brand outcome.

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its significantly, so the question has to be asked: will they pass on their financial pain to retail pharmacy in the form of lower discounts and reduced service levels to make up for the shortfall?

'I estimate that over the next 12 months, the three wholesalers will collectively lose sales from switching and the 12.5 per cent price clawback of between $250m and $300m,' he said.

'Multiply that by a gross profit margin percentage of, say, 5 per cent, and we can see that the profit impact is around $13m. They simply can't afford that, which means, because brand pharma has been hit too, retail pharmacies may have to face up to copping a reduction in wholesaler trade discounts plus services reduction and/or having to pay more.'

'Make no mistake. All three wholesalers are affected so it won't be as easy as in the past for pharmacies to play one wholesaler off against the other to defray the negative bottom-line impact of these Government policies,' asserted Mr Annabel.

And added to all this is the significant time required from pharmacy staff to explain all these changes to customers.

Of course, many consumers prefer the brand product and they constitute the great majority of pharmaceutical items sold (about 76 per cent). The solution is to replace the lost dollars through (as encouraged by the Government) increased generic substitution.

For pharmacies to achieve maximum discount terms, they will need to become more relevant to suppliers and wholesalers, Mr Annabel said.

'So choose a first-line wholesaler and generic manufacturer to whom you will commit most of your business in order to get the most "discount" in return. While the generic manufacturers will be a volume beneficiary and, hence, be in a better position to absorb some, or perhaps all, of the profit they will lose from maintaining pharmacy owners discount percentages as they are, only time will tell,' said Mr Annabel.