

News

3 Reasons Why Amazon Invaded the U.S. Pharmacy Industry

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Pharmacy Industry%0D%0A"Amazon is like a shark, and this is what it feeds on."%0D%0A%0D%0Ahttps://www.equities.com/news/3-reasons-why-amazon-invaded-the-us-pharmacy-industry)



Amazon (AMZN (<https://www.equities.com/companies/amzn>)) is the original giant killer in the digital age. Whenever Amazon invades into a new business area, their laser like focus to cut prices and provide value to the end user, heralded the end of the road for incumbents. When Amazon started to sell Kindle and books online, Borders went from \$1.6 billion (<http://www.sfgate.com/business/article/How-Amazon-factor-killed-retailers-like-6378619.php>) of revenue to bankruptcy in 2011.

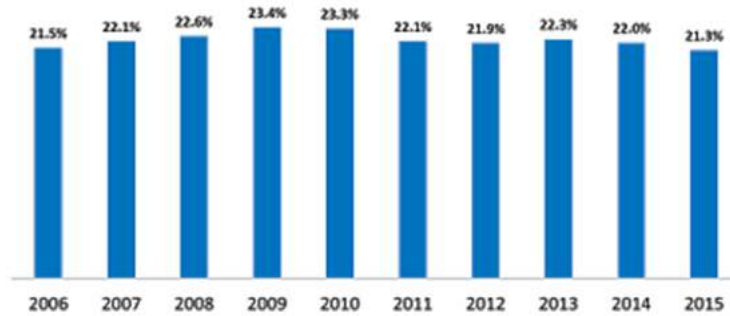
Amazon was part of the e-commerce revolution with peers such as eBay (EBAY (<https://www.equities.com/companies/ebay>)) and Alibaba (BABA (<https://www.equities.com/companies/baba>)), which took a major portion of the consumer's wallet share and resulted in the demise of brick and mortar stores such as Circuit City. Amazon's entry into the cloud and groceries businesses are less dramatic but they had shaken the industry.

Today, Amazon had chosen to invade the pharmacy business in the United States after having gotten licenses from 13 states and counting. The only question today would be how disruptive Amazon would be and why it had chosen the pharmacy business instead of trying to manufacture cars for example.

Fat Margins

Amazon is like a shark that can be counted to be present whenever they smell the blood of fat margins. Pharmaceutical Journal (<http://www.pharmaceutical-journal.com/careers-and-jobs/career-feature/ever-wondered-whether-owning-your-own-pharmacy-is-worth-it/10989400.article>) wrote a detailed thesis on pharmacy finances and encouraged graduating pharmacists to start their own business. According to their calculation, product profit margins can go up as high as 100% and with the careful arrangement of products and financing, it is almost certain for a new pharmacist to be profitable.

Average Prescription Gross Margins at Independent Pharmacies, 2006-2015



Source: Pembroke Consulting analysis of *The NCPA Digest*, various years; Pembroke Consulting estimates. Note that data have been restated compared with previous estimates.

Published on Drug Channels (www.drugchannels.net) on December 13, 2016.



Source: *Drugs Channels* (<http://www.drugchannels.net/2016/12/new-data-show-prescription-profits.html>)

CVS (CVS (<https://www.equities.com/companies/cvs>)) reported a gross margin of 29.4% (<http://www.todayonline.com/business/drugstore-chain-cvs-reports-better-expected-profit>) even when they are facing government pressures to reduce drug costs and competition from Walgreens (WBA (<https://www.equities.com/companies/wba>)) this year. CVS reported \$44.51 billion of revenue and \$952 million of net income in one quarter. Looking beyond the big players, independent pharmacy operators are also earning good income. For single store owners, they make an average of \$247,000 per year (<http://exclusive.multibriefs.com/content/are-independent-pharmacies-really-that-profitable/pharmaceutical>). On average, the independent store owners have 3.6 stores which allows them to make \$900,000 per year.

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2. Synergy with Prime and Retail Stores

Physical retail stores provide a good synergy for pharmacies. For instance, Wal-Mart (WMT (<https://www.equities.com/companies/wmt>)) had leveraged on its 4,672 physical stores (<https://www.statista.com/statistics/269425/total-number-of-walmart-stores-in-the-united-states-by-type/>) in the US for its Walmart Pharmacy (<https://www.walmart.com/cp/pharmacy/5431>) brand. Amazon has a number of physical stores (<https://www.amazon.com/b?node=14303222011>) around the United States which is boosted by its Whole Food acquisitions. This would allow Amazon Pharmacy to expand naturally. Amazon is known for its automated warehouses which can be staffed by qualified pharmacists which can interact with patients through telepresence robots, taking a leaf out of 3E Accounting's practice (<https://www.3ecpa.com.sg/press/1st-accounting-firm-to-implement-double-robotics-technology/>).

Even if patients don't want to visit the physical stores, Amazon can use their same day Prime service to make the delivery to their doorstep. Currently, with just \$35, Amazon customers can get free same day delivery (<https://www.amazon.com/Prime-FREE-Same-Day-Delivery/b?node=8729023011>) to 7,000 cities and towns in the United States. Amazon can also upsell health books to its drugs customers on the relevant topics.

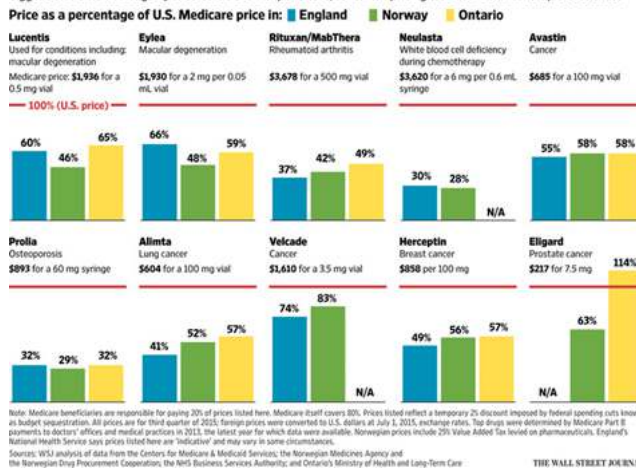
3. Customer Outrage Over High Drug Prices

Pharmaceutical companies such as Turing Pharmaceuticals, Retrophin Inc. (RTRX (<https://www.equities.com/companies/rtrx>)), Valeant Pharmaceuticals International (VRX (<https://www.equities.com/companies/vrx>)) and Rodelis Therapeutics were in the spotlight last year for their practice of drastically increasing prices (<http://beta.latimes.com/business/la-fi-senate-drug-price-study-20161221-story.html>) to make more profits. Mylan (MYL (<https://www.equities.com/companies/myl>)) increased the price of EpiPen (<http://www.businessinsider.sg/mylan-ceo-heather-bresch-hearing-on-epipen-2016-9/?r=US&IR=T>), needed for allergic treatments by 500%. One of their strategy of preventing generics manufacturers would be to use specialty pharmacies to restrict supplies.

High drug prices still persist in the United States and they are being challenged legally by states such as California (<http://fortune.com/2017/10/10/california-drug-prices-pharma-sb17/>). The new California law would force pharmaceutical companies to explain if they increase their price by 16% over 2 years but it is not expected to reduce prices. The longevity of the of the law is being question as it would be challenged in the courts.

Same Drug, Higher Price

Here are prices the government health systems of England, Norway and Ontario, Canada, paid for some of the biggest brand-name drugs by Medicare Part B expenditure, for which pricing was available in multiple countries.



Source: Wall Street Journal (<https://www.wsj.com/articles/why-the-u-s-pays-more-than-other-countries-for-drugs-1448939481>)

Governors and lawmakers are unlikely to force drug companies to clean up their act (<https://blog.fantasticcleaners.com/burn-calories-while-spring-cleaning/>) and reduce medical costs. As noted by WSJ, drugs are simply more expensive in the US than other western and developed countries and this finding is echoed by Bloomberg (<https://www.bloomberg.com/graphics/2015-drug-prices/>). Given that the authorities are powerless against the established power of Big Pharma, Amazon is the last hope in forcing lower prices from Big Pharma (<http://www.alabamane.wsj.com/2017/11/05/amazon-threat-causes-shakeout-health-care-industry/>).

Shake-Up

The Amazon entry into the pharmacy business is good news to consumers but bad news for shareholders of existing pharmacy and pharmaceutical companies. The only question is whether these companies would go the way of Borders or the way of Walmart. CVS is already offering same day delivery (<http://www.chicagotribune.com/business/ct-biz-cvs-prescription-drug-delivery-20171106-story.html>) in response to Amazon's threat and this is only the beginning.

The giant killer is here and a shake-up is not necessarily a bad thing for the industry which badly needs it.

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Companies

	Symbol	Name	Price	Change	%	Volume	
Follow	BABA	Alibaba Group Holding Limited American Depositary (/companies/baba)	181.79	-2.75	-1.49	14,475,342	\$ Trade
Follow	WMT	Wal-Mart Stores Inc. (/companies/wmt)	91.09	0.10	0.11	9,834,133	\$ Trade
Follow	VRX	Valeant Pharmaceuticals International Inc. (/companies/vrx)	14.28	-0.32	-2.19	16,274,449	\$ Trade
Follow	EBAY	eBay Inc. (/companies/ebay)	35.22	-0.63	-1.76	11,468,030	\$ Trade
Follow	AMZN	Amazon.com Inc. (/companies/amzn)	1,136.84	7.67	0.68	3,138,423	\$ Trade
Follow	RTRX	Retrophin Inc. (/companies/rtrx)	21.34	-0.01	-0.05	226,897	\$ Trade
Follow	WBA	Walgreens Boots Alliance Inc. (/companies/wba)	70.59	0.22	0.31	5,268,978	\$ Trade
Follow	CVS	CVS Health Corporation (/companies/cvs)	70.44	-1.04	-1.46	5,964,036	\$ Trade
Follow	MYL	Mylan N.V. (/companies/myl)	37.85	0.28	0.75	3,732,870	\$ Trade

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