VETERINARY PRACTICE PARTNERS

VETPulse

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AN UNBIASED LOOK AT THE TRENDS AFFECTING TODAY'S PRACTICES

In This Issue

Revisiting Flea, Tick and Heartworm Revenue Growth

In the first edition of VetPulse in early 2012 we examined trends in the sales of Flea, Tick and Heartworm (FTH) medications in veterinary practices. At the time, the commonly accepted view was that internet competition and big box retailers had materially hurt veterinary practice sales of these products. However, data from 2007 to 2011 showed that FTH revenue for practices was actually still growing, at an even faster pace than overall practice revenues. However, the data did suggest that profit margins on FTH were being negatively impacted.

Chart 1 Annual Growth of Flea, Tick & Heartworm Revenue vs. Total Practice Revenue

We took a look at more recent data from hundreds of veterinary practices and found very similar results. Despite the increased competition, our data shows that revenue from FTH products is still growing, though at a slower rate – a 0.6% compounded annual growth rate from 2009 to 2013, down from 2.5% from 2007-2011 (Chart 1). Despite this growth, 75% of practices surveyed continue to believe that they have lost revenue from reduced product sales.

The findings from our survey speak to the strategies adopted by many practices to combat the competitive pressure of outside retailers:

- **63%** of practices have re-trained their staff to better communicate the benefits of buying the products at the veterinary practices
- **54%** of practices are consciously focusing on service-based revenues and less on product sales
- **41%** of practices have lowered prices on FTH products
- **39%** have changed their available product mix

Our survey looked at changes in FTH revenue, not in the number of units sold. Since almost half of our respondents have lowered prices to compete with online and big box retailers, we believe that unit volume has likely increased at a faster pace than revenue, despite the perception to the contrary.

"Revenue from FTH products is still growing, though at a slower rate"

For survey participant demographics and study methodology, see page 4

When asked about responding to requests for signatures on FTH prescriptions, only 35% of practices say they sign and fax the prescription to an internet retailer without first attempting to convert the client. Before signing and faxing the prescription:

- **26%** of practices call the client to discuss the benefits of purchasing directly from the hospital
- **24%** of practices write a prescription that must be picked up from the office
- **18%** of practices call the client to discuss and match the internet price

Our Recommendations

At Veterinary Practice Partners, we encourage all of our practices to offer a product mix that includes a combination of online and offline-only FTH products. We train our staff to articulate the benefits of buying from a veterinary practice specifically highlighting the product guarantee from manufacturers that 1800 PetMeds cannot offer and to price match anyone submitting a script for approval. We also regularly create promotions around the sales of these products in conjunction with the manufacturer rebates.

We believe in maintaining foot traffic and having purchases made through our practice instead of elsewhere, even at a lower profit level. Remember, as long as you are making some profit on the product, you are better off than losing the sale altogether and having the client purchase from somewhere other than your practice. Our preferred product mix includes one well-known brand name that consumers may be loyal to and another product that is very difficult to obtain on the internet. While the increased competition from internet providers and big box retailers is frustrating and results in lower profit margins, it is essential to keep your clients loyal to your practice by having them come to your practice for as much of their pet's heath care (and other) needs as possible.

Manufacturer Market Share in Veterinary Practices

The biggest change from the 2007-2011 data has been in the practice's FTH product mix and market share, calculated as the percentage of FTH revenue from each specific product and manufacturer.

Since 2010, Elanco, the animal health division of Eli Lilly, has grown by an impressive 150% to achieve a comfortable 20% market share, second only to Merial (Chart 2). Elanco's growth is even more dramatic considering we found that in 2008 its share was only 2.3%. In April of this year, Lilly announced a proposal to purchase the weakened Novartis and merge it with Elanco to create the second-largest animal health company in the world.

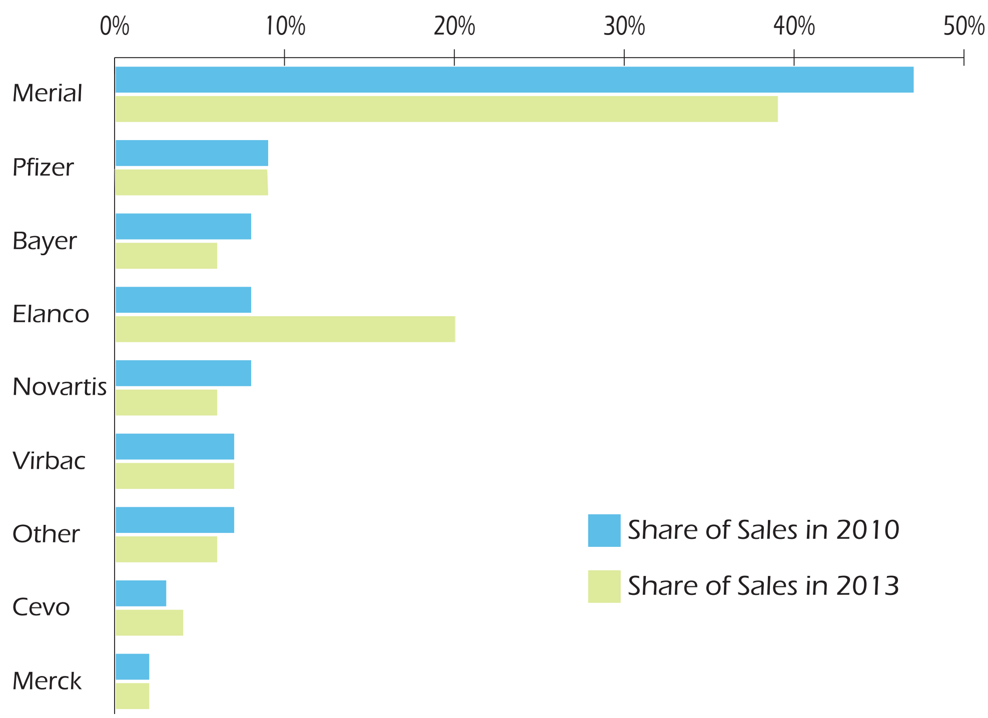
"The biggest change from the 2007-2011 data has been in the practice's FTH product mix and market share"

As you may recall, Novartis was forced to take Interceptor and Sentinel off the market due to manufacturing issues relating to other products at the only U.S. plant that manufactured Interceptor and Sentinel. When they were able to get FDA clearance to re-launch the products, Novartis decided to discontinue Interceptor altogether and re-launch Sentinel at a lower price point to recapture market share. Since the re-launch, Novartis has achieved about 6% market share.

Some veterinarians reported enough frustration with Novartis to decline to promote the re-launched Sentinel to their clients and instead have adopted Elanco's Trifexis or a combination of other products.

With the potential Elanco-Novartis merger going forward, Elanco will be in a strong position to offer veterinary practices both a high-cost and low-cost product mix.

Chart 2 **Manufacturer Share of Practice Flea, Tick & Heartworm Sales**



Merial, who started 2008 with a strong 53% market share in veterinary practice product sales, decreased sharply from 2008-2011 and has since stabilized at approximately 39% in the past three years. In the next two years, we should be able to see whether NexGard, which came out on the market this spring, will be able to bring Merial back closer to its former majority share. Our survey found that 13% of practices currently carry NexGard and, of those who don't, only 24% have plans to carry it in the future.

Market Growth Statistics

As part of our commitment to educating veterinarians on market trends, we include market growth data in each issue so you can compare your practice with industry benchmarks. We analyze revenue growth from VPP practices, VCA and IDEXX's data that is a proxy for the market.

The first quarter of 2014 saw a deceleration in growth due to the harsh winter, in comparison to the milder 2013 winter (Table 1). IDEXX, VCA and VPP practices all bounced back to a strong second quarter. As the number of VPP hospitals increases, we expect our growth to normalize to about 2-3% above Market.

"The first quarter of 2014 saw a deceleration in growth due to the harsh winter"

TABLE 1 **Year-over-Year Revenue Growth**

	2012		2013				2014	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
VCA Antech	1.1%	1.6%	1.8%	1.3%	1.1%	0.9%	1.1%	2.2%
IDEXX (Market Proxy)	6.0%	5.0%	3.5%	4.9%	6.1%	5.2%	2.1%	4.3%
VPP	11.8%	13.2%	11.5%	10.8%	12.2%	11.0%	10.8%	13.4%

Survey Methodology

The survey was conducted by a New York City-based market research firm. The survey questions presented in this newsletter were part of a larger ongoing market tracking study which has been conducted for several years to assess changes and trends impacting veterinary practices. Practice-wide metrics captured in this survey, including monthly revenue data, is provided directly from electronic practice management systems. The survey is not affiliated in any manner with any veterinary product manufacturer.

"The survey is not affiliated in any manner with any veterinary product manufacturer."

Region	All Practices in Sample Set *(n=181)*	Universe of Practices in US *(n=32,755)*
New England	3%	5%
Middle Atlantic	8%	10%
East North Central	17%	15%
West North Central	17%	10%
South Atlantic	19%	19%
East South Central	5%	7%
West South Central	8%	13%
Mountain	11%	8%
Pacific	12%	14%

Practices were recruited randomly from a universe listing of veterinary practices provided by InfoUSA, a leading provider of medical databases. During April 2014, 181 veterinarian practices participated in this survey, of which 65% were veterinary practice owners, 19% were office managers, and 16% were non-owner DVMs or had other titles. The practices participating in this research represent a good regional cross section of the country as illustrated by the table above. Additionally, from a total practice revenue standpoint, those surveyed are very similar to the national averages:

Practice Revenue	All Practices in Sample Set *(n=181)*	Universe of Practices in US *(n=32,755)*
Under $700,000	45%	59%
$700k to <$1.5 million	40%	27%
$1.5 million - <$3 million	13%	11%
Over $3 million	2%	4%

VETERINARY PRACTICE PARTNERS

Rich Lester, CEO

About Veterinary Practice Partners

VPP is a management company in the veterinary industry; we buy ownership stakes in practices and then work behind the scenes to manage and grow those practices. VPP handles marketing, accounting, human resources and vendor contracting so our DVM co-owners can focus on patient care. Working together as partners, VPP and the DVMs make all major business decisions.

For more information on our unique approach to managing veterinary practices, and to learn how we might be able to help your practice meet its goals, please contact us:

- Visit our website at **www.vetpartners.com**
- Give us a call at **866-VET-PART (838-7278)**
- Send us an e-mail at **info@vetpartners.com**