

# Using 867 Data: Tracking Your Key Indirect Customers

By Doug Linton, President, Consulting

Trade directors at branded pharmaceutical manufacturers are challenged by the tendency for retail pharmacy chains to supply their distribution centers through wholesalers. Without accurate and timely sales data, trade directors often find it difficult to fully understand the impact of their indirect chain customers. Furthermore, this group's (chains, mass merchandisers and grocers) position as the largest class of trade – representing more than 44% of total Rx sales – mandates the development of an in depth knowledge about these indirect customers (see Table A: Rx Sales By Trade Group on page 2).

In today's Fee for Service (FFS) environment, wholesalers are making the data related to sales and purchases available as part of the FFS negotiation process. This data is contained in what is formally known as Product Transfer Activity, although it is more commonly called 867 data.

The fact that sales and purchases data can be obtained raises the question:

**How does a pharmaceutical manufacturer stay on top of what these large indirect customers are doing and what is the reward for doing so?**

The answer to the first part of this question is straightforward. Most of the high-volume branded Rx products are stocked by the chains in their own warehouses. Typically, a wholesaler sells these products to chain warehouses through one of two business models:

- 1. Brokerage/Dock-to-Dock** – The chain places an order with the wholesaler who turns around and places the order with the manufacturer. When the order is delivered to the wholesaler, it is not inventoried, but instead it is loaded on a truck within 24 hours for delivery to the chain's warehouse. Payment terms are normally a certain number of days less than the terms on the manufacturer's invoice.
- 2. NEXT DAY DELIVERY FROM STOCK** – Unlike the Brokerage model, the wholesaler maintains inventories so a chain's warehouse orders can be shipped within 24 hours of receipt. The result is lower inventories at the chain warehouse. Some wholesaler distribution centers (DCs) are designed to only supply chain warehouses, while others supply warehouses and individual pharmacies.

**Table A: Rx Sales By Trade Group**

	Dollars (\$mil)	Market (%)
Chain & Mass Merchandiser	\$84,132	35.70%
Independent Pharmacy	\$33,410	14.20%
Mail Service	\$33,877	14.40%
Hospitals	\$28,377	12.10%
Clinics	\$21,887	9.30%
Food Stores w/pharmacy	\$20,755	8.80%
Nursing Homes/Home Health	\$10,605	4.50%
Other	\$2,325	0.90%
<b>Total</b>	<b>\$235,367</b>	<b>100.00%</b>

Source: 2005-2006 HDMA Fact Book. IMS National Sales Perspective (2004)

The Brokerage model requires the chain to carry additional inventory, due to less frequent ordering and longer lead time compared to the Next Day Delivery model. The choice of model shifts the responsibility for the carrying of inventory to either the wholesaler or the chain. Obviously, the Brokerage model will make the chain more aware of the length and consistency of the manufacturer's lead times. In contrast, the Next Day Delivery model cushions the chain from variations in manufacturer service.

## GETTING THE DATA

Since 867 data can be made available under today's FFS agreements, the manufacturer should request all elements of data between the wholesaler and its customers, including returns. While this data is accumulated daily, it may be reported to the manufacturer daily or weekly.

Assuming 867 data can be obtained, the next challenge is to get it in a form that is useful for reporting and analysis. Because products that are sold to chain warehouses are also being sold to thousands of independent pharmacies nationwide, a request for a wholesaler's 867 data for a portfolio of products will generate a large amount of data. Daily transactions are usually small and numerous. Most wholesalers provide this data in a standard EDI format once a week. A mid-tier manufacturer with up to twenty SKUs can easily receive 50,000 lines of data a week from each national wholesaler. As an alternative to in-house software development, many manufacturers are opting for third party solutions that support the collection and analysis of this data.

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## What to look for – “Old Worries”

As manufacturers have told us - confirmed in various consulting projects - the “old” business model involving speculative buying and secondary market activity is still alive among some chains. We were involved in a recent project where a chain stopped buying a particular manufacturer’s product from a wholesaler immediately after a price increase and did not resume buying it for a number of weeks. This made a material impact on the wholesaler’s purchases from the manufacturer and made sales forecasting from shipments data a very challenging activity since script data from other sources delivered a conflicting outlook.

While we believe the wholesaler may be innocent in these situations, the manufacturer should contemplate whether to amend FFS agreements to hold the wholesaler more accountable for the actions of its customers. In the meantime, manufacturers will sleep better at night knowing their indirect customers’ purchases are monitored for the telltale peaks and valleys around pricing actions using 867 data.

## What to look for – “New Worries”

If the chains have moved away from the “old” business model, they may still have business practices that can impact the distribution channel. The practice of balance sheet cosmetics at the end of a reporting period can create ripple effects throughout the channel, as shown below:

Similar scenarios can develop when chains alter their order patterns as the result of changing warehouse supply business models or decisions about what products to stock in their warehouses.

## Benefits from Using the Data

Collection and analysis of 867 data for key indirect customers can produce numerous benefits to the pharmaceutical manufacturer and trading partners.

- 1. More Accurate Sales Forecasts** – Sales forecast surprises can be avoided by knowing what actions the big indirect customers are taking around price increases and at the end of financial reporting periods. It is important to understand the impact of acquisitions compared to same store growth.
- 2. Happier Key Customers** – Keep these large customers happy by knowing how your most important products are performing for them. Customers appreciate it when you know what is going on with their business.
- 3. Better Product Availability** – When a large customer

sneezes, other customers can catch a cold! Monitor large customer purchasing patterns and related supply issues to avoid an epidemic among other wholesaler customers.

- 4. More Insight into Returns** – Monitoring and analyzing returns in the 867 data can provide insight into the sources and reasons for returns. Our analysis has shown there can be dramatically different returns profiles for each wholesaler.
- 5. More Fair FFS Agreements** – Changing chain warehouse supply relationships and business models can significantly impact the volume of wholesaler purchases and the cost of supplying their customers. These changes should be reflected in your FFS agreements with the wholesalers.

## CONCERNS

**BLINDED DATA.** Wholesalers have stated that some contracts with customers preclude including detailed 867 data or possibly identifying their customer. We suggest that this shortcoming is worth pursuing with the wholesaler and/or the chain as there may be less sensitivity about chain warehouse purchases than purchases of individual stores. Chains may want visibility around their purchases to have a more meaningful dialogue with manufacturers on problems and opportunities.

**INACCURATE DATA.** Manufacturers have a right to expect that the data they pay for is accurate. As this is a relatively new area for wholesalers, it is possible that the data may not initially reconcile. Detailed 867 data should reconcile to aggregate 852 data even though they may not be generated from the same wholesaler internal systems. Some manufacturers have reported monthly variances exceeding 10%. It is strongly recommended that data synchronization be an integral part of any efforts to use this data for sales forecasting or other monitoring activities. Data synchronization involves both matching the numbers on 867 and 852 data and confirming the reasonableness of 852 data by performing a roll forward exercise to compare actual to projected inventory levels.

## SUMMARY

The pharmaceutical distribution channel continues to be dynamic. Today’s trade management team needs accurate and timely information about major indirect customers to be able to monitor for speculative buying, provide daily customer support and assess changes in supply chain strategies. With the availability of 867 data and powerful data analysis tools, it is possible to monitor indirect customer purchase activity almost as if they were buying direct.