Learning Organisations & Knowledge Management

- Firms' CA depends more than ever on what it knows, how it uses what it knows, and how quickly it can learn something new
- Firms that support & encourage knowledge management are called Learning Organisations—demonstrate sustained CA over rivals
- CA is sustainable when it persists despite efforts by competitors or potential entrants into market to duplicate it or neutralize it

Categories of Innovation

- In every industry, leading competitors are innovators
- Real challenge: sustained innovation

1. **Improving Core Businesses**
   - Focuses on incremental innovations that can be developed rapidly and inexpensively
   - Includes line extensions & more convenient packaging—often part of a horizontal growth strategy
   - Potential weakness is its focus on current products and customers.
2. **Exploiting Strategic Advantages**
   - Focus: takes existing brands and product lines to new customers and markets without requiring major change in current capabilities
   - Moves beyond the company's current strategic scope by leveraging capabilities by spreading them across a broader range of markets and customers.
   - Potential weakness is in the relative ease with which competitors with similar capabilities can imitate the innovation.
3. **Developing New Capabilities**
   - Focus: deepening customer satisfaction and loyalty to the brand or product line by adding new organisational capabilities without introducing major changes in strategic scope.
   - Company may develop or purchase new technologies to better serve the firm's current scope of customers and markets.
   - Potential weakness is in the investment cost and implementation time.
4. **Creating Revolutionary Change**
   - Focuses on radical innovations that transcend current product lines or brands to make fundamental changes in both its strategic scope and its capabilities.
   - Potential weakness is a high risk of failure

Summary

- One of the primary causes of business failure is the pharmacist's inability to develop goals and strategic plans.
- Objectives provide overall direction. Policies give general guidelines. Procedures are specific statements that describe how the policies are to be carried out to achieve goals.
- Developing goals, plans, policies, procedures requires planning at all levels for a period of time.
- Obstacles to planning are inability to set goals, inexactness, variability and lack of time.
- A Business Focus makes sure that the monetary, human and material resources of the pharmacy are used most effectively.
- A good pharmacist does not just focus on the clinical aspects of the profession BUT understands the business and economic environments within which they work as well.

<u>Financial Management</u>

- Spend management, cash management, resource management, revenue management, supplier management, financial accounting
- The determination, acquisition, allocation and utilization of financial resources
- Aim: achieve firm's strategic objectives
- Understanding essential to: business staying afloat or working within budget, able to take adv of business opportunities, achieves sustainable competitive adv
- i.e. implementing new service
  - financial planning required
    - funds required, services to cover operational costs, where to obtain funds, current profits to cover loan until profitable
- Quantitative: involving numbers
- Qualitative: observed, not translatable to numbers
- Ensures necessary financial resources are available to achieve goals & objectives determined by strategic planning process
- Concerned with generation & management of value-enhancing cash flows (cash flow problems are cause of majority small business failures)
  - Cash inflow: revenue from sales
  - Cash at hand: decreases
  - Cash outflow: cost of production
- Looking at revenue and number of prescriptions coming in is not an indicator of success
- Objectives
  - Profitability: above average returns. Yield a rate of return commensurate with level of risk involved
  - Liquidity: ensuring there is always a sufficient cash available to pay bills (cash flow)
  - Capital structure: healthy balance between debt & equity in long-term fund arrangement
    - Debt finance: external
    - Equity finance: internal (firm owners/shareholders)
    - AKA level of financial gearing or financial leverage
- Key to:
  - Bonuses, Promotion, Success, understanding business & Understanding your accountant
- Competition for patients and resources
  - Hospitals—competition with other organisations for budget sharing
  - Community—fight for the share of market (competitive and profitable)

Net profit margin (%)	▪ Gross profit plus other income minus the expenses incurred ▪ ↓ net profit margin over time: o ↑ expenses w/o corresponding ↑ in sales (i.e. rent or wages) o ↓ sales or income from other sources without ↓ corresponding expenses (i.e. Rx income drops due to price disclosure)	
EBIT ($)	▪ Earnings before interest & tax ▪ Preferred over net profit due to varying interest rates overtime, thus remove interest rates get a better idea of trends/fluctuations due to purely operational causes ▪ Provides better comparison of firms and how well they operate	
EBIT margin (%)	▪	
Expense component ratio (%)	Selling expense ratio (%) ▪ ↑ can mean o ↑ in advertising costs which may or may not benefit future sales o ↑ in number of sales staff which may or may not be warranted Administrative expense ratio (%) ▪ May be rent or utilities ▪ Not directly related to the sale of goods	
Asset turnover ratio	▪ Measures relationship of sales to total assets ▪ Dependent on valuations used for assets so care required when comparing 2 companies as timing and method may differ ▪ Supermarket expected to have higher asset turnover ratio than furniture store ▪ Must benchmark, otherwise ratio means nothing ▪ ↓ in asset turnover ratio over time an analysis	
Return on investment (ROI) (%)	▪ “does a higher turnover compensate for a lower profit margin?” ▪ ROI > 0 (or > 0%) means investment returns more than its cost ▪ Higher ROI is better choice or business decision (between investments competing for funds or when other factors b/t choices are truly equal)	
GMROII	▪ Gross margin return on inventory investment ▪ A seller’s income for every dollar spent on inventory (higher the better) ▪ Important in community pharmacy where stockturn (inventory turnover) & gross margin % can vary by item, location and week ▪ Main driver for pharmacy owners to analyze product and store offering ▪ Advantages o GP margin % an be distorted by high volume (high sales) items which have low margin, or if pharmacy has high inventory. GMROII looks at margin return on avg inventory as opposed to sales it tends to give better indication on performance o High GMROII = good balance of sales, margin and inventory costs (COGS). Pharmacy’s benchmark in in 300 percentile range or ratio of 3 (300% or 3)	
Inventory turnover (stockturn)	▪ Measures the efficiency of inventory management → number of times per yr inventory is turned over into sales ▪ To convert to no. days stock is held: o Low → poor management → inventory costs high, may be obsolete stock (hard to sell) o High → good management or business not keeping adequate stock lvls thus lost sales & excessive restocking costs o COGs in the formula and not sales b/c stock is recorded at cost price & not selling price (which may change over the yr, changing inventory turnover ratio artificially w/o influencing inventory management	
Current asset ratio	▪ Working capital ratio ▪ Working capital is the difference between current assets and current liabilities ▪ Most businesses operate between ratio of 2 and 6 ▪ High asset ratio is not necessarily good: could mean excessive current asset holdings due to poor inventory turnover or accounts receivable or assets that might be better turned into investments	
Quick assets ratio	▪ Excludes less liquid current assets and less pressing liabilities ▪ Different from current asset ratio is the speed which a conversion to cash can be made ▪ Normally excluded from current assets are inventory and hire-purchase items (can’t be converted to cash easily)	
Breakeven sales ($)	▪ Cash flow ratio: measure of short-term liquidity → can business pay its current liabilities? ▪ AKA breakeven point ▪ Level of sales where no profit or loss is made (ignore other income), at this point business breaks even ▪ Net profit at this point = 0 Amended formula: Net profit = Gross profit – Total expenses (not considering other income) Gross profit = Total sales – COGS At breakeven point: Total sales – COGS – Total expenses [Use net profit here, because want to include interest paid in calculations]	

Pricing Strategies

- Depends on what type of demand there is for product or service
- Demand can be elastic or inelastic
  - Elastic
    - Change in price has a significant effect on the demand i.e. ↑ price, customers may choose not to buy
    - Dependent on # of factors
      - Product a necessity or a luxury?
      - Substitutes available?
      - Complementary products? (price of one product ↓, demand for another product ↑ i.e. razors & shaving cream)
  - Inelastic
    - Price change has little effect on demand i.e. customers still buy regardless of price

- **Premium** pricing
  - High quality, premium product – priced at highest acceptable cost to consumer before they look for a substitute product
  - Strategy: 'Image Pricing'—perceived image is more important to a customer than the actual price (i.e. high-quality brand over a cheaper copy)
  - Customers willing to pay more b/c of value they place on product
- Market **Penetration** pricing
  - Aims for high sales through a lower price
  - Often used for products & services that would not attract an initial elite market
  - Discourages competitors b/c of low profit margin
  - Large target market & high volume of sales are needed to meet profit goals
  - High quality but price might be kept ↓ to drive out competition I.e. loss leaders → raise price later when competitors are driven out
- **Economy** pricing
  - Aimed at the budget end of the market where customers are willing to forgo some quality or service for a lower price
  - Difficult to use LT—sales volume must be consistently high to maintain good profit lvls
- Price **skimming**
  - Often used for new products and services, esp. tech
  - Initial price is set high & attracts 'early adopters' who want the product or service now & are willing to pay
  - When group is satisfied, price is reduced to appeal to more price-sensitive customers
- Strategies

Business level	Cost leader	Differentiator	Integrated cost leadership/differentiator
Marketing	Product orientation	Marketing orientation → marketing w/ superior lvl of service	Market orientation → relationship marketing
Pricing	Economy and market penetration	Premium with some skimming when they are selling stars	Skimming when they are selling stars market penetration and some economy (unlikely to use premium pricing)

Recap: importance of benchmarking

- Process of continual improvement, if changes implemented should benchmark business again to see results (tell you what's working & how you can still improve)
- Strategy tool used to compare the performance of the business process and products with the best performances of other companies inside and outside the profession—process of comparison
- Important tool in strategic management to improve performance—gives essential info abt how you can improve your business
- Analyse in detail how your business compares to others
- Many ways to benchmark your business:
  - Used financial benchmarking data to
    - Compare business' income, expenses & profitability against industry avgs
    - Examine financial data of similar businesses
  - Use data from Pharmacy Guild (you must be a member) to measure performance against other industry standards
  - Research and compare business' products, services & practices with your competitors
- Used to:
  - To reveal successful business processes – review how other pharmacies perform so highly, can apply same processes, skills & competencies
  - To facilitate knowledge sharing – knowledge acquired by studying other businesses can be transferred to own
  - To gain competitive advantage – if apply best practices from other industries to own industry
- Helps you to
  - See where costs can be reduced, and improved efficiency
  - Assess productivity of business cf to how many employees you have
  - Identify opportunities for improvement, new ideas & innovative practices
  - Highlight opportunities for making your business more competitive
  - Forecast impact of any changes & see how to prepare for growth
- Possible discoveries
  - Spending too much on rent and need to consider negotiating lower rental rates
  - Higher inventory costs than your competitors → may need to ↓ waste or negotiate better rates from supplies
  - Income per employee lower than industry avg → examine productivity and training