

Walgreens: Strategic Analysis

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Introduction

Walgreen Co. first opened its doors for business one hundred and five years ago, operating a single store in Illinois (Frederick, June, 2006). Today Walgreens is America's most successful drugstore chain, operating a network of over 5,500 stores in forty-seven states and Puerto Rico (Walgreens, October 2006). Moreover, their success is spreading; Walgreens is opening a new store more than once a day- netting 371 stores in 2005 (Frederick, June 2006). However, top competitor CVS has surpassed Walgreens in terms of store numbers, topping 6,000 locations following their purchase of the Eckard empire. Still, Walgreens is the "unchallenged leader" in profits, profits per square foot, prescription sales per store, and newly built stores (Frederick, June 2006 and Drug Store News, October 2006).

This past August, Walgreens notched their 32 consecutive year of record sales and earnings. On the year, sales rose 12.3 percent, climbing to \$47.4 billion, while they also reported same-store sales gains of 7.7 percent. Obviously, for drugstores, prescription sales are of great importance to the success of the business. For Walgreens, prescription sales accounted for nearly 65 percent of total sales in 2006, up 13.3 percent compared to 2005 (Drug Store News, October 2006). Aside from prescriptions, Walgreens continually works to grow customer satisfaction in the front end by assembling the right product mix. According to former Walgreen Co. CEO David Bernauer, "one reason that we can continue to grow is that our earnings per square foot are \$46, while drug chains average less than half of that" (Frederick, June 2006). Despite the change in management, it's expected to be business as usual under newly appointed CEO Jeff Rein, a 24-year Walgreens veteran.

Over the course of its 105 year life, Walgreens has been a retailing leader, producing satisfied customers and healthy bottom lines. However, due to the competitive nature of their industry, Walgreens must overcome new challenges daily to remain the industry leader.

Strengths

Walgreens knows what they're doing; they wouldn't be the most profitable drug store chain if they didn't. Walgreens' biggest strength is their knowledge of their customers. For instance, they know that their customer prioritize convenience; therefore they implement a saturation style store expansion plan to insure that customers are close to a Walgreens, because if not, they won't shop there. According to Rein, the company is well on its way to operating 7,000 stores by the target date of 2010 (Drug Store News, October 2006). Furthermore, Walgreens has a competitive advantage over CVS because nearly all of the new Walgreens stores are freestanding and built from the ground up, ensuring that there in highly visible locations.

Furthermore, Walgreens has done a great job at responding to the changing demands of their customers. For example, they have begun a rebranding project in the makeup department by transforming the departments' look with new store displays and improving service with specially trained beauty advisors. Most importantly, the merchandise is new. Their European Beauty Collection is comprised of seven lines, totaling 130 products, from countries like France, Spain, Greece, and Switzerland (Edger Michelle, Andrea Nagel, June 2006). In addition, Walgreens recently announced the introduction of a new fashion jewelry line. The Pure Allure Crystal Collection will feature world-renowned Swarovski crystals. The collection will be include 36 core

styles, as well as seasonal styles that hit store shelves every six weeks. These changes reflect Walgreens' effort to meet the demands of their female customers, who are "both fashionable and price savvy" (Walgreens, October 2006).

Walgreens has responded to consumer demands in other ways. For instance, Walgreens recently introduced inkjet cartridge refilling stations in approximately a fourth of its stores, making it feel like an office superstore within a drugstore. Customers can drop their cartridges off at the photo shop, shop, then pick them up ready to go, at half the cost of a new cartridge (Troy, April 2006). Other improvements are taking place in Walgreen's photo shop thanks to a partnership with Fujifilm. Through Fujifilm's website, www.yourpix.com, consumers can choose to pick up their prints at more than 5,500 locations nationwide for just 19 cents per print. Even more convenient is that 1,500 locations are open and offer this service 24 hours a day (Walgreens, November 2006).

Change is also taking place in the back of the store. Following the acquisitions of C&M Pharmacy and MedMark, Walgreens is working to open in-store clinics staffed by nurse practitioners, providing access to quick and affordable healthcare for its customers. The clinics charge between \$25 and \$60 per visit and offer customers routine medical services, screenings, and immunizations without making an appointment beforehand (Drug Topics, January 2006). Recently, Walgreens debuted their Health Corner Clinics to the Atlanta market, opening in 16 locations around the city (Walgreens, November 2006).

Lastly, Walgreens is the leading drug store chain because of their commitment to innovate. For example, Walgreens is a pioneer of energy conservation among retailers;

they installed solar panels on 96 stores and two distribution centers in California, and 16 New Jersey locations. The result: generating 13.8 million kilowatt-hours per year (energy equivalent of 22 million gallons of gasoline) and the completion of the largest solar energy project in the United States (Drug Store News, May 2006).

Additionally, Walgreens is the first drugstore chain in the nation to introduce radio-frequency identification (RFID). RFID allows Walgreens the ability to watch the status of in-store displays for all the stores. Doing so will help Walgreens' managers analyze the sales impact of in-store advertising in real time, providing an opportunity to quickly adjust the merchandise on a store to store basis (Wilson, February 2006).

Overall Walgreens has several strengths that make it a leading American retailer. Their customer knowledge, ability to adapt to the needs of their customers and to be a marketplace innovator is one reason they have been so successful.

Weaknesses

Despite their many competitive advantages, Walgreens does have weakness in their operation. For instance, the layout of most stores is in grid format, which should theoretically help customers find what they're looking for easily. However, at Walgreens, this layout doesn't make finding products any easier; too many items are crammed into too small of a space that finding the right product is often difficult. With less space than larger retailers, it's important for Walgreens to carry the most optimal product mix because larger retailers like Target are afforded more leeway with their product categories because of their size, yet can still satisfying the customers' desire for convenience.

In addition, the aisles in Walgreens are so narrow it's difficult for customers to walk down them without bumping into other customers. Outside the store, traffic jams are prevalent as well. In most locations, the store occupies a corner lot, with parking spaces surrounding the building. These lots are not wide enough, making it difficult to pull in and out of the parking spaces. To compound the problem, cars speeding through the lot heading for the drive through sneak up on cars pulling out. To make matters worse, there is a lot of pedestrian traffic around the building. The problems with the store layout and small parking lots make visiting Walgreen's a bit less convenient.

Furthermore, Walgreens has the same problem as many other retailers: impolite sales people. For the most part, retail employees have little knowledge of the products in their store, or if they do know, they're usually too preoccupied with their tasks to help the customer. Also, at the checkout, rather than being courteous to the customer they're helping, cashiers socialize with other employees working near them (Personal visit to Walgreens locations, December 5 and 6, Cincinnati, OH). Although Walgreens tries to provide incentive for their employees by promotion within the company, it's still a problem that they face (Drug Store News, March 2006).

Another weakness of Walgreens is with their traffic generator: medicine. This industry is very dynamic; however, it's strictly regulated by volumes of technical rules. In order to legally sell prescription drugs, Walgreens must constantly stay up to date with all of the latest regulations of the drugs. Furthermore, they must also be experts on the drugs themselves in order to effectively counsel their customers. In an effort to become experts of the pharmaceutical industry, Walgreens must allocate more resources to this task, thus allocating less to directly satisfying customers. If Walgreens fails to be up to

date on even the smallest industry standard, the threat of a major lawsuit will surely result.

Lastly, prescription medicines are so expensive that insurance companies are needed to pay for the drugs. Therefore, for Walgreens to receive payment for their product they must maintain relationships with third party insurance customers, otherwise they will lose customers. Essentially, their ability to satisfy some customers is at the mercy of a third party.

Fortunately, the other drug store chains have many of the same problems as Walgreens. Therefore, if they're able to address these weaknesses, then these problems become competitive advantages.

Opportunities

Although working in the pharmaceutical industry can create a few problems, it also presents many opportunities for Walgreens. For example, the first wave of "baby boomers" are reaching the age of retirement, thus the demand for prescriptions drugs is ready to explode even more. This presents a huge opportunity for Walgreens. Also, the fact that this market is financially stable and able to withstand major cost increases is an added bonus (Confectioner, December 2006). Walgreens know this. In an effort to reach this viable market, Walgreens has formed a partnership with the AARP, providing members with co-branded health and wellness brochures and community education programs (Frederick, October 2006).

Obviously, Walgreens will face stiff competition for this lucrative market segment. Therefore, there is an opportunity to target younger customers, who need

medicine as well. By doing so, Walgreens can create a lifetime customer, and a relationship that will exist for decades (Confectioner, December 2006).

Walgreens is a leader in distributing prescription drugs; therefore customers associate Walgreens with a healthy lifestyle. Walgreens has several opportunities to capitalize on this reputation. For instance, in terms of nutrition, opportunities exist for Walgreens to expand its product mix into the health food segments, such as fresh fruits and vegetables and organic product lines. At the 2006 Consumer 360 Conference retail executives agreed that the consumer awareness of “health and wellness is a long-term trend,” not just another fad. With this new demand opportunity is knocking on Walgreen’s door because of their trusted name in the industry (Azzalo and Longo, June 2006). In addition to medicine, opportunities exist for Walgreens to take advantage of their trusted brand name by offering more private label brands (Drug Topics, January 2006). These products will increase customer loyalty because they’re only available in one place. Also, private labels don’t have manufacturers’ restrictions on price and display, and they have higher gross margins (Levy and Weitz, 2007).

Finally, every new Walgreens location that opens represents a new opportunity. In these communities Walgreens wants to establish themselves as a neighborhood pharmacy (Walgreens, October 2006). In order to establish themselves as a community brand, Walgreens should provide add-on services that customers may not be used to. For instance, some small pharmacies will deliver medications to their customers, saving them the hassle of going out in the cold while they’re sick. Also, something as simple as knowing the names of your best customers will connect the store with the neighborhood.

In the end, the best opportunities are ones that ultimately benefit the customer because if pursued, will likely contribute to financial success.

Threats

As a leader in the drug store industry, Walgreens' expects to be the target of many threats. Their response to these threats is a primary reason Walgreens remains an industry leader.

First of all, Walgreens faces a threat from major retailers like Wal-Mart and Target, who have introduced generic drug discount programs. In September Wal-Mart rolled out a test program to offer 30-day supply's of 300 generic medications for \$4. The program is designed to steal customers, however, according to Walgreens, "95 percent of our pharmacy patients have prescription insurance coverage, meaning their only responsible for a small co pay." Furthermore, Walgreens stocks around 1,800 generic medications (Walker, November 2006).

Secondly, Walgreens faces political threats. Recently, Congress passed cuts to Medicaid's pharmacy reimbursement plan, leaving Walgreens with less incentive to fill these prescriptions because of the cut in profit margin. If this adjustment to Medicaid passes, Walgreens will lose thousands of customers and garner a lot of negative publicity (Drug Store News, March 2006).

There is also the threat of lawsuits. Lawsuits are a possibility for anyone; however, due to the nature of pharmaceuticals, the likelihood of a liability suit is higher. As a member of the supply chain, Walgreens can expect to be served just because by selling the product, they endorse it (Drug Topics, February 2006).

Although Walgreens needs the pharmaceutical companies for their business, these companies can also negatively affect Walgreens bottom line. For instance, if pharmaceutical companies don't introduce as many new drugs to the market, Walgreens will be forced to sell more generic drugs, which have lower profit margins (Drug Store News, March 2006).

Finally, Walgreens faces a more traditional threat-direct competition. Case in point, Walgreens and CVS are currently engaged in an arms race for store locations. Both drug chains are aggressively trying to acquire drugstores to expand their company's customer base. Recently Walgreens bought into the Delaware market by purchasing Happy Harry's, while CVS acquired Sav-on and Osco, expanding by 700 locations (Datamonitor, August 2006). With more emphasis on convenience in the drugstore industry than others, more locations pay dividends of customer satisfaction and actual profits.

In conclusion, they're many threats to the success of Walgreens; ranging from direct competition from retailers such as Wal-Mart and CVS, economic slowdowns affecting front end sales, and mild winters preserving customers' health.

Recommendations

In order to improve, Walgreens must fix the areas in which they're weak. First of all, they need to improve the layout of their stores. Walgreens should keep the grid format because of its convenience, but reduce the clutter of displays in the aisles. In addition, more prominent signage above the aisles will help customers locate the products they're looking for. By reducing the clutter, shopping at Walgreens will not only be more convenient but feel friendlier as well.

Outside, Walgreens should redesign their parking lots. Although their parking spaces are close to their buildings, parking isn't too convenient because of the amount of traffic in the small area. They should make the parking lot wider to reduce the risk of traffic accidents and make stopping in more convenient. A simple solution to remedy the problem of cars speeding through the parking lot is to add speed bumps at the entrances to get cars to slow down.

Although comprehensive training programs are not common for retailers, Walgreens should develop one for all current and newly hired employees. If employees are trained in multiple departments and rotate positions, then employees can work in other departments during slow periods. Secondly, rotating departments will break up the monotony of their jobs, increasing employee happiness. The result will be increased productivity and customer satisfaction.

In addition to fixing their weak areas, Walgreens needs to continue to grow in their areas of strength. Walgreens use of RFID technology to analyze the effectiveness of store displays demonstrates that they're leaders in this area. Walgreens should expand their use of RFID technology because the amount of valuable customer information they will receive is tremendous. For example, Walgreens will be able to tell exactly where a product has been throughout the supply chain, even after it leaves the store.

In conclusion, Walgreens must stay focused on what got them to the top-customer satisfaction. If they get caught up with the financial statements and look for new ways to cut costs, they will inevitably cut out customer satisfaction.

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