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Sick Pharmacies may need financial restructuring

The last 12 months have been difficult for retail pharmacists with virtually all pharmacies having suffered at least a 25% reduction in their gross profit margin. In addition, the volume of sales has tumbled significantly. The economic downturn has dramatically hit front of house sales and now many pharmacists are wishing that they had smaller retail units. Only 24 months ago, it was not unusual to have pharmacists seeking 1,500 square foot premises but, now a small dispensing space is very much more in vogue.

Due to increasing financial difficulties, a number of pharmacy retailers have had to wind up their companies in recent months, with some high profile casualties. In addition, drug wholesalers have come under financial pressure. These difficulties are as a result of the HSE cuts in payments to both pharmacy wholesalers and retailers. Celesio, who own Unicare and Cahill May Roberts in Ireland recently reduced the value of its Irish pharmacies by €85 million and prominent pharmacies, such as Hamilton Long on Dublin's O'Connell Street recently went into liquidation. Unfortunately, we expect many more pharmacies to encounter trouble after the Christmas period. If the gearing is too high or the rent is unsustainable then it is time to start looking at restructuring options. The sooner it is started, the more likely it is to be successful.

If all of the above was not bad enough, the fact is that many pharmacies are too highly leveraged with debt. This is particularly the case with pharmacies that were either acquired as going concerns in recent times or, indeed green-field pharmacies, which are located beside primary care centres. In 2006 and 2007, we saw acquisitions of pharmacies at valuations of 30 times net profit and this did not even include the pharmacy premises. Purchasers who borrowed to fund acquisitions on these types of multiples must be feeling the pain - and facing the problem is part of the remedy.

So, after outlining the difficulties it is worth pointing out that many businesses are undergoing balance sheet

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restructurings. These range from examinerships (where Court protection is placed over the company) to informal schemes of arrangement where write-offs of debt are agreed with creditors in a voluntary way. Restructuring a company can be likened to a patient going through a life saving operation.

The first phase of the process is the diagnostics (e.g. MRI scan). The business rescue practitioner assesses the status of the business like an MRI scan for a patient. Having determined the extent of the problem with the patient, the surgeon performs the life saving surgery. In a similar way, the business rescue practitioner may need to close down part of the business, slash costs and so on and this is the business surgery. The patient then enters the post-operative phase and is in step-down care and monitored closely. Again, in business terms the turnaround practitioner performs less critical things like strengthening the management and monitoring closely the trading performance of the company. Finally, when the operation is well over, the patient is encouraged to adopt a healthy lifestyle and so it is in business also, where processes and systems are developed to keep the business strong.

One key area of concern for retailers, and particularly pharmacists, is in respect of rents. Onerous leases of property are now causing many businesses to fail.

Many landlords have recognized this and are willing to renegotiate leases downwards. For those landlords who are not willing to accept reasonable renegotiations of leases, their tenants face the likelihood of having to seek examinership protection, or go into liquidation.

Under examinership legislation, there is a provision whereby the company can seek the repudiation of an onerous contract. This has been utilised in a number of instances to either get rid of a troublesome lease or, indeed as the stimulus to get the landlord to agree to a rent write-down. In the Chartbusters case, Judge John Edwards allowed the repudiation of a number of leases. In contrast to this, however, is the O'Brien's Irish Sandwich Bar case when the High Court did not approve the repudiation of over 40 leases.

In summary, many sectors of retail in Ireland are feeling the pinch and the norms of 2006 and 2007 are a distant memory. Some of the financial structures adopted in those good times have to be altered today and the sooner these realities are faced by businesses the better are their prospects of survival. Banks and landlords are recognizing more and more the need to adopt supportive stances and well presented restructuring strategies are being received favourably.

