

Drugstore.com

by

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Abstract

This research paper takes an in-depth look at Drugstore.com. First, opening day is discussed. Second, a look into the person(s) behind this online phenomenon is highlighted. Third, a behind the scenes look is detailed. Next, a glimpse at the marketing plan along with the competition is analyzed. Lastly, laws and regulations are detailed as it relates to Drugstore.com.

Drugstore.com

Five letters spell relief - drugs. There is not a bathroom cabinet in America that does not have some kind of drug in it. Whether it is aspirin, cold pills, or prescribed medicine, drugs are a part of everyone's life. Prescription drug costs increase an average of 16 percent a year. Consumers, such as you and I, are bearing much of the financial burden. "Even health care coverage's bite-size prescription co-payments of \$10 or \$20 in some cases are being jacked up as much as \$50" (Bond, 1999).

"Indeed, for every dollar Americans spent on books last year, they spent four on prescription and over-the-counter medications, industry executives estimate. The drugstore totals: \$90 billion on prescriptions, \$20 billion on over-the-counter health goods, \$20 billion on personal care items, \$20 billion on vitamins and other 'wellness' products, and \$15 billion on beauty aids and cosmetics" (Tedeschi, 1999). Even the federal government predicts Americans will spend vast amounts on drugs. By 2007, it is estimated that Americans will spend as much as \$171 billion a year (Bond, 1999).

This billion-dollar industry is unparalleled for the Internet. It only makes sense that health related services, such as Internet-based pharmacies, are being touted as the next big thing online. "While many businesses are looking to the Web to generate revenue, those in the health care space are particularly well-positioned to take advantage of all that the Internet has to offer" (Kornblum, 1998).

Most of the e-commerce dollars have gone to sites selling universal products such as books, music, and computers. "The last holiday shopping season proved people will click to buy books, music, and videos online" (Net pharmacies preparing..., 1999). The majority of Americans are tired of getting the bureaucratic runaround from their managed-care networks. They are hungry for ways to get more information about health and health care products (Kornblum, 1999).

To appease this hungry fever, the Internet seems to be the next logical step. The Web is turning into one big medicine chest. "Online drugstores and natural health and vitamin sellers are popping up faster than crocuses in spring, aiming to do well by keeping people well. Granted, cough and cold remedies aren't practical to shop for online: who'd wait through days of sniffles for FedEx to bring help? What electronic pharmacies and nutrition stores are counting on, though, are consumers to turn to Web-based sources for chronic-health prescriptions and staples such as vitamins, toothpaste, cotton balls, and deodorant" (Livewire: Net Drugstores seek..., 1999).

Besides, visiting the local pharmacy can be embarrassing. "Who wants to walk up to a cash register with a bottle of Rogaine, a pack of condoms and an assortment of wrinkle creams, particularly when Mildred from down the block might be lurking in aisle two?" (Stone, 1999). "It's a market trend. Seventy-six million baby boomers are all going to be over 40 by the year 2004 and health will start to play a more important role. 'Being young

and beauty are going to be very important', says Michael Tchong, editor of *Iconocast*, a Internet marketing newsletter" (Online Drug Shopping..., 1999).

"Industry watchers said the online pharmacies will have an initial advantage by bringing a fresh perspective to the business and an understanding of how best to use technology in retailing. E-mail reminders of when it's time to refill prescriptions, personalized stores based on a customer's interest and integration of medical information with the sale of products, for example, may give online stores an edge" (Net pharmacies preparing..., 1999).

One online store is taking the leading edge in health care. It is Drugstore.com. Drugstore.com seems to be the future pharmacist. "There are a number of deep-pocketed people who believe the pharmacist of the future will turn out to have an electronic heart" (Tedeschi, 1999). Drugstore.com has the biggest head start in the Web-only health care newcomers. "The Seattle start-up, which opened its 19,000 item electronic health emporium in February, is backed by nearly \$60 million from Silicon Valley venture capitalist Kleiner Perkins Caufield & Byers and is 40 percent owned by e-commerce all-star Amazon.com" (Livewire: Net Drugstores seek..., 1999).

This research paper takes an in-depth look at Drugstore.com. First, opening day is discussed. Second, a look into the person(s) behind this online phenomenon is highlighted. Third, a behind the scenes look is detailed. Next, a glimpse at the marketing plan along with the competition is analyzed. Lastly, laws and regulations are detailed as it relates to Drugstore.com.

Opening Day

"If the wave of publicity got Drugstore.com execs excited about their grand Web opening last week, then the crush of traffic that ensued probably had them popping Valiums. Drugstore.com officials were mum on total numbers, but in a Reuters feed, VP Suzan DelBene speculated that 10 million people would have visited on the first day of business if not for the site's 'front-end' limitations" (Mendel, 1999).

The front door was flooded. Many potential customers were denied entrance into Drugstore.com. Thursday, February 25 had marked the day when Drugstore.com did not have enough capacity to handle all the customers. The front door is flooded said Suzan DelBene, vice president of the new online drugstore. The site had been designed with plenty of back-end capacity but was limited on the front-end. "DelBene said the strain on the site resulted from a rush of visitors beginning early in the day. If the early day rate of visits to the site continued, it would total 10 million visitors by the end of the day" (Reuters, 1999).

What had consumers rushing to their computers? "Drugstore.com will offer not only prescription drugs but also most of what consumers would find in a CVS or Rite Aid:

over-the-counter drugs, cosmetics, vitamins, toothpaste and shampoo, all delivered to your door" (McCollum, 1999). However, it is just not the items listed above that Drugstore.com has to offer. They are also offering information. There is a resource center right online. Therefore, if there are questions regarding health, beauty, and wellness, Drugstore.com wants to help locate an answer and a product too.

Background

Drugstore.com did not become a reality until February 1999. However, it was an idea that started in November 1997. Jed Smith, a former Oracle executive, is the company founder. "Smith developed the idea for Drugstore.com and approached Kleiner Perkins for funding. The venture firm is the sole backer of the new business" (Kawamoto, 1998). Smith was also the creator of the brick-and-mortar cybercafe called Cybersmith. Jed Smith serves as the vice president of Drugstore.com.

Kleiner Perkins Caufield & Byers (KPCB) put the Drugstore.com project into its "Entrepreneur in residence" program. This is an incubator for early stage companies. "KCBP's CEO-in-residence program has existed for about 20 years and is designed to recruit CEOs for companies that it finances" (Kawamoto, 1998). Then KCBP went searching for that special CEO.

It was in July 1998 when headlines started announcing that a Microsoft Executive was leaving. Peter Neupert was chosen as CEO of Drugstore.com. "Peter Neupert, a key member of Microsoft's new-media executive team, will leave the software developer to become the CEO of an undisclosed start-up" (Microsoft loses media VP, 1998).

Peter Neupert is not new to start-up ventures. "He played a key role in founding MSNBC's Internet and joint cable ventures, as well as the management of Slate. He also headed advertising and sales for Microsoft's online properties" (Pelline, 1998). Neupert had an 11 year tenure with Microsoft.

"Neupert believes that the key to success will be to emphasize the convenience - an anonymity - of shopping on the Internet. 'It's better to get condoms in a box than at the checkout line', he said. In general, he added, 'the drugstore experience today isn't a pleasant one'" (Richtel, 1999).

One of Neupert's first goals was to build up his management team. "It lists Tracy Nolan, former vice president of Merck-Medco Managed Care, as vice president of operations; Suzan Fine DelBene, a former Microsoft executive, as VP of marketing; Kal Raman, former CIO of NationsRent, as VP and CIO; and Andy Stergachis, a professor of pharmacy at the University of Washington, as director of pharmacy services and quality assurance" (Pelline, 1998).

Along with this elite management team comes Amazon.com and Starbucks Chief Executive Howard Schultz. "Amazon, which owns 46 percent of Drugstore.com will promote the new site with links throughout its service and through e-mail to its customers. But the two stores will be otherwise separate. Thus, a flu sufferer will not be able, in one transaction, to order a decongestant and a novel. Amazon's involvement was orchestrated by John Doerr, the influential venture capitalist at Kleiner Perkins Caufield & Byers, who had been an early backer of both companies. Last summer, Doerr convinced Jeff Bezos, Amazon's chief executive, to invest in Drugstore.com and to serve on its board" (Hansell, 1999).

In late February, Jeff Bezos raised \$1.25 billion in a junk-bond offering to buy Amazon's share of Drugstore.com. "There are a lot of differences between books and drugstores, Bezos says, but there are a lot of similarities too. Customers want selection, convenience, price, and information. He says Amazon.com will share management tips with the company and encourage Amazon's visitors to try the new pharmacy" (De Jonge, 1999).

Starbucks Chief Executive Howard Schultz agreed to buy a stake in Drugstore.com too. "Schultz declined to disclose the size of his purchase, which will give him a seat on the company's board. Schultz is buying the stake through his private investment company, Maveron LLC. 'Drugstore.com is at the forefront of the latest generation of e-commerce', said Schultz" (Reuters, 1999).

Behind the Scenes at Drugstore.com

Two main business operations must be flawless, appealing, and convenient for customers to shop at Drugstore.com. They are the web site and distribution system. The web site is the only storefront ever seen by the customer's eyes. Therefore, it has to draw customers in. On December 9, 1998, Interactive Bureau won the Drugstore.com account to design the web site. A special office was set up in the Seattle area just to manage this project.

"John Sanford, former Creative Director of MSNBC, was recruited to lead the new Interactive Bureau Seattle office and will head up the design team for Drugstore.com. 'We needed Internet design consultants that could deliver a great shopping experience and understand our unique business requirements', said Peter Neupert. Interactive Bureau, a leading Internet design consulting firm, was founded in 1994 by distinguished print designer Roger Black and veteran media Jock Spivy" (Drugstore.com chooses..., 1998).

Along with a great web site comes a great distribution system. When dealing with drugs, the company must ensure that the right customer gets the right drugs. "At issue is a perfect shipping record of health goods to the end consumer, an insurance of applications installed by ScanData at the Drugstore.com distribution facility. 'The pack and ship point is the last check on order accuracy and represents the last impression for the customer with the arrival of the order', said John Dalton, president of ScanData. Drugstore.com requires a system with zero percent errors."

"ScanData installed the system of clients, workstations, and production server within weeks of signing a contract with Drugstore.com. Shipping Automation and order verification applications were installed as part of the system. These two suites of products are licensed for Microsoft BackOffice and recognized by Microsoft with four Retail Application Development (RAD) awards" (Drugstore.com implements..., 1999).

Marketing

Since Drugstore.com now has a great web site and distribution system, a marketing plan was needed. "The race to be the most visible health site is well under way. With so many players in this fast growing market, online health care businesses need to build brands, reputations, connections - or enough financial backing to buy all three - or they're just going to be another flash in the bedpan" (Harvey, 1999).

Recently, Drugstore.com has announced deals with AOL, Excite, and Yahoo. On February 16, 1999, Drugstore.com had distribution deals with AOL. "Under the terms of America Online (AOL) deal, once it is launched, Drugstore.com will be a featured online pharmacy in America Online's health area and a variety of other channels including travel, families, sports, and lifestyles. Terms of the AOL and Drugstore.com deal were not disclosed" (Kawamoto, 1999).

Drugstore.com had also signed a sponsorship agreement with Excite. "Drugstore.com will have links, text links, text module boxes and banner advertisements on the Excite portions of Netscape's Netcenter Network, including shopping and health-related pages. And Drugstore.com plans to run other promotional campaigns on the Excite portions of Netscape's Netcenter site. 'Excite's relationship with Netscape allows us to reach Netscape's strong member-based community and provides Drugstore.com with another excellent distribution channel', said Peter Neupert, president and CEO of Drugstore.com" (Cox, 1999).

Lastly, Drugstore.com struck a deal with Yahoo in late February 1999. Promotions include merchant buttons and banner ads on the portal site. "The duration and financial terms of the deal were not disclosed" (Martin, 1999).

Are portals the way to go? "Clearly, despite the fact that sites are climbing over each other to sign deals with Internet portals, the game of getting people to trust a Web site for health information will reach far beyond the Internet. As with other Internet businesses, analysts feel that the more pull a Web site has offline, the better its chances of staying online" (Harvey, 1999).

However, not all analysts feel this way. "Spurning the portals may not be so foolish after all", said Melissa Bane, an electronic commerce analyst with the Yankee Group, a Boston-based consulting firm. 'Is Yahoo the best place for a prescription company to

advertise? Who knows? I think it remains to be seen', she said" (Tedeschi, 1999). "Every household has health/medical issues; therefore, health is a category likely to enjoy portal status" (Kornblum, 1998).

Competition

"Since the new year began, Internet drugstores have grown at an amphetamine-like pace" (Daragahi, 1999). Drugstore.com has many rivals including other online drugstores, traditional chain companies, and mail order companies.

Other Online Drugstores

"Several well-funded online drugstores are jockeying for position in this nascent market." Soma and PlanetRx are two major online competitors to Drugstore.com. "Soma, founded by Tom Pigott, heir to a truck manufacturing fortune. PlanetRx backed by Sequoia Capital, has Federal Express management muscle behind it in CEO Bill Razzouk, the former executive vice president of worldwide operations for the shipping company" (McNaughton, 1999).

On January 15, 1999, Soma.com opened its web site doors. Soma is based in Seattle, Washington. "In addition to dispensing prescription medications, Soma will also sell over-the-counter drugs, vitamins, health care products, health and beauty aids, and alternative remedies. Once the pharmacy receives and verifies the prescription with the patient's health provider, Soma promises delivery at prices often below those at major chain drugstores. The company will emphasize superior pharmacy services and health information, which will allow it to deliver a level of customer service rarely found at large drugstores or on the Internet" (Soma.com, the first major..., 1999).

In total, Soma offers about 15,000 drugstore items. "'Soma dispenses to 32 states and has been adding about five states a week,' said company spokeswoman Sandi Sonnenfeld. The online pharmacy is open 24 hours, and pharmacists are available to answer questions. Orders in plain packaging are shipped to your doorstep. The site also sends e-mail reminders about refills and, for customers who request it, e-mail reminding them when to take their medication" (Isaacs, 1999).

PlanetRx is in a new biotechnology building located in South San Francisco, California. Bill Razzouk, a former VP at FedEx, is the CEO of PlanetRx. It features typical drugstore health and beauty items. Along, with Drugstore.com and Soma.com, PlanetRx also has a 24-hour pharmacy service.

These online drugstores have a distinct advantage over the traditional retail chains. "Because they have no brick-and-mortar pharmacy, online pharmacists' can charge between 20 and 30 percent less for drugs than retail chains. Patients who take drugs covered by insurance companies and shell out the same co-payment regardless of cost

won't be attracted to the Web stores. But price will make a big difference for over-the-counter medication and prescriptions such as birth-control pills not covered by most insurers. For this group, Web drugstores will be an easy pill to swallow" (Daragahi, 1999).

Traditional Chain Companies

Traditional chain companies are not sitting idly by either. They are fighting back. "Some offer limited online refill services, and No. 3 Rite Aid has plans to roll out a prescription and vitamin website with GNC in the fall" (Elsenberg, 1999). "Giant Rite Aid, CVS, and Walgreens already allow their customers to refill prescriptions online, although they still have to go to the local store for pickup. These sites also offer services like e-mail refill reminders" (Brakeman, 1999).

Other traditional stores are doing much of the same. Drug Emporium operates an online drugstore. Longs Drug Stores recently cut a deal with planetU to provide visitors to its Web site with coupons they could print out and bring in to brick-and-mortar stores. Wal-Mart offers an array of health and beauty products in its Web store. Kmart kicked off its Web presence selling vitamins. "Walgreens already runs an Internet site that lets customers order and check on the status of their prescription refills, which they then pick up in a local Walgreens store. Its expanded site will offer full-service ordering and delivery for all prescriptions and some other goods including health and beauty products and vitamins" (Walgreens to sell..., 1999). Even Peapod is joining the online health care market. "Online grocer Peapod said on Tuesday it plans to branch out into the drugstore business by selling goods from Walgreens, the largest drugstore chain in the United States" (Bicknell, 1999).

Is Drugstore.com worried? Not hardly. "That doesn't worry Drugstore.com's Neupert, who says, 'Frankly, I don't know if the existing brands are all that respected'" (Elsenberg, 1999).

Mail Order Companies

Many health insurance companies rely on generic and mail-order companies. "One obstacle is the fact that many health insurers hire outside firms to perform mail-order subscription re-fills. Since online pharmacies essentially perform the same service as mail-order companies, some insurers won't welcome the competition" (Tedeschi, 1999).

"The online drugstores say that since mail-order pharmacies control 10 to 15 percent of the market - and not all have exclusive agreements with insurers - these services won't prevent Internet ventures from succeeding" (Tedeschi, 1999). "But Web drugstores also offer something not found at most mail-order outfits - information" (Daragahi, 1999). Drugstore.com, for example, will be open all the time, dispensing not only pills but also advice from pharmacists.

Laws & Regulations

In the arena of laws and regulations, online drugstores may have an uphill battle. This is over and above Drugstore.com's zero percent policy for order shipment. "Beyond distribution, online drugstores have other pills to swallow, not the least of which is the tangle of licensing regulations governing who can sell prescription drugs. Laws covering mail-order prescription sales vary by state: What's legal in some, isn't in others" (Rafter, 1998).

This online selling of drugs is not going unwatched by the government either. The embryonic online prescription drug business is coming under scrutiny from federal watchdogs and professional organizations such as the National Association of Pharmacy Boards. There are reports that some companies allow customers to purchase powerful prescription medicines such as Viagra and Propecia with nothing more than an online 'visit' to a virtual doctor (Rubin, 1999).

According to the National Association of Pharmacy Boards, if there were not a legitimate patient to physician interaction at the site, then that site would be practicing pharmacy illegally. One of the major concerns is sites that allow patients to answer a few brief questions and then fill a prescription. "Precipitating the scrutiny of the online stores, however, is the practice by some of them of not only filling prescriptions but also providing physicians to write them for patients who do not have their own doctors" (Rafter, 1998).

Privacy and accurate medical information are other problems. "Other important issues are protecting consumers' privacy and giving them appropriate medical information. Given the sensitivity of prescription information - and the potential damage that could happen if information falls into the wrong hands - stores need to take extra steps to make sure that information is secure. Customers of some online vendors wanting to buy Viagra, for example, can obtain the anti-impotence drug by filling out online questionnaires that are reviewed by doctors for potential problems. There is no way to guarantee the information's accuracy, however" (Rafter, 1998).

The rapidly exploring trend of online pharmacies is clearly outpacing laws and regulations. "But the situation could improve in short order. With so many companies targeting the online selling space, state pharmacy boards are updating laws to better address Net and mail-order sales" (Rafter, 1998). In addition, online drugstores such as Drugstore.com, Soma.com, and PlanetRx.com are teaming up to urge stricter enforcement of existing laws. "It's a bad result if good guys get tarred with the brush meant to be applied to the bad,' Soma.com spokesman Mitchell Reid said. 'The good guys have absolutely nothing to fear from tough enforcement of laws that are on the books'" (Clark, 1999).

Conclusion

This research paper analyzed Drugstore.com. From opening day to laws and regulations, each business aspect was highlighted. Opening day had proven to be a success with an estimated 10 million visits. A behind the scenes look was centered on the web site development and distribution system. Marketing was the next business aspect discussed. One quote sums up the marketing strategy. "Online, as in the real world, the key to success is location, location, location. The winners in the online drugstore race will likely be the ones who spend big on advertising and sew up promotional deals with portal sites" (Rafter, 1998). Drugstore.com was not oblivious to this. They had deals with AOL prior to Web opening day. Next, competition with other online drugstores, retail chains, and mail-order companies was analyzed. Lastly, laws and regulations was briefly described. Drugstore.com has urged stricter enforcement of laws and regulations. They believe they are the good guys.

Will Drugstore.com reign king in the online health world? I think that still remains to be seen. However, it is not as if they do not have the experience or intelligence to become the next e-commerce superstar. They have an excellent entrepreneur leading the way. "It just means a fairly brutal war, with a lot of promising companies beaten into submission. If it's any consolation - and it probably isn't - the losers should at least be able to handle the pain" (Tedeschi, 1999).

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