



# **UNDERSTANDING MONGOLIAN PRIVATE VETERINARY UNITS AS SMALL BUSINESSES**

**Analysis and Recommendations for Improvement**

JUNE 2018



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# Introduction

Private Veterinary Units (PVUs) are the key field actors for the Mongolian animal health sector. In rural Mongolia, PVUs are the primary contact points for herder households who want to access veterinary services. However, PVUs are essentially small businesses and their ability to provide consistent and quality service depends on the same questions that apply to other small businesses:

- **Is the business feasible in its operations?**
- **Is the business profitable in its operations?**

This report aims to investigate both these questions in regards to PVUs. It analyzes overall feasibility and profitability of PVUs, barriers to PVU growth in these areas, and develops a series of recommendations for increasing PVU profitability based on the analysis.

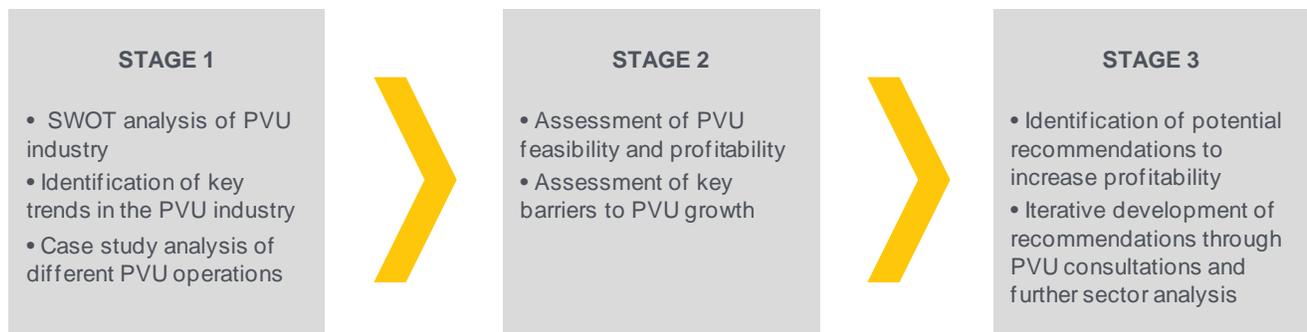
By mapping the financial and operational profile of PVUs and exploring the potential opportunities for improving their profitability this report hopes to inform future initiatives aiming to improve PVU operations in Mongolia and by extension the operation of Mongolia's animal health sector.

## Methodology

The analysis follows a three-stage methodology. The first stage focuses on collecting data on the PVU industry and collecting data on specific PVU operations across a variety of different operational contexts. The second stage involves analyzing the collected data to make an assessment of general PVU feasibility and profitability and key barriers to PVU growth. The third stage involves utilizing the outputs from the prior stages to develop a series of recommendations for PVUs to increase their profitability.

The sample size of PVUs interviewed was eight. This is acknowledged as a small number however efforts were made to ensure interviewed PVUs represented a cross section of PVU operations. Rural and urban PVUs were interviewed and PVUs came from four different aimags. We believe the interviewed PVUs are diverse enough for a general understanding of the fundamentals of PVU operations.

**Figure 1 | Analysis Methodology Summary**



### Profitability Against Feasibility

**Feasibility:** is a question of whether the costs incurred in an operation are covered by the revenues (including required return). Feasibility implies the operation can perpetuate.

**Profitability:** since feasibility only focuses on breakeven financials, the follow up question is how profitable the operation is. Reasonable profitability is critical for, among other things, the long-term growth of the operation as it allows reinvestment to grow the operation. Profitability implies the operation can flourish.

# Key Findings

## PVU Feasibility and Profitability

### PVU Feasibility

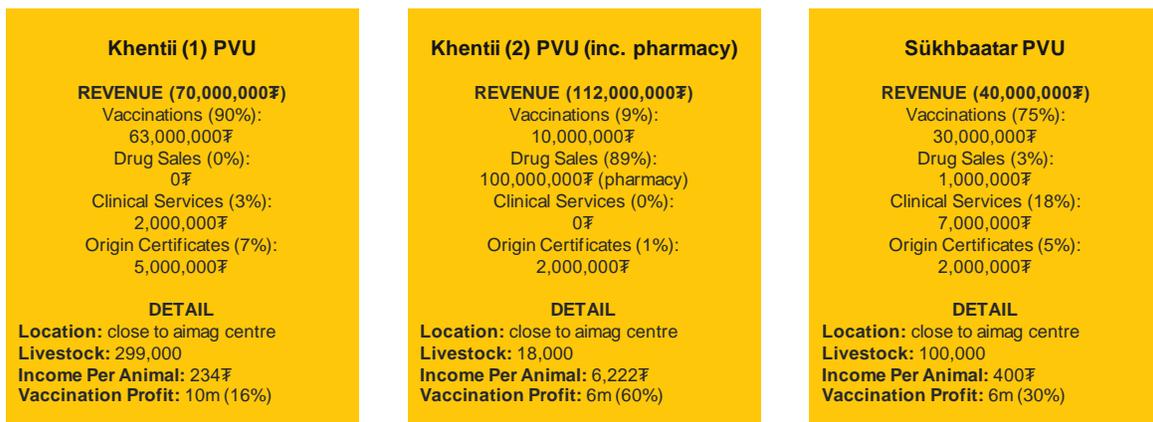
PVUs are financially feasible through several sources of reliable income including vaccination services, origin certificate provision, and certain clinical services e.g. anti-parasitic services. However, feasibility for certain PVUs is tenuous due to delays in receiving income. The key delays are created by herders paying for services on credit and by the government delaying its payment of vaccination service fees to PVUs. These delays result in PVUs having to take out loans or having to utilize their personal savings to manage the cash shortfall, compromising their feasibility.

### PVU Profitability

Profitability among PVUs depends on their operational context. The report analyzed a range of PVUs across different operational contexts (see figure 2). The following key impacts on profitability were noted:

- Operational context affects how profitable key PVU activities are. For example, the second Khentii PVU and the Sukhbaatar PVU have higher profitability for vaccination services because their herder households are close to the aimag center and are close to each other, leading to lower fuel costs. The first Khentii PVU, on the other hand, has to travel more when providing vaccinations.
- Operational context affects the volume of certain activities. For example, certain areas have frequent disease outbreaks/larger livestock numbers leading to a higher volume of vaccination services (see first Khentii PVU). Conversely, some PVUs operate in contexts where the vaccination services volume is significantly lower due to minimal disease outbreaks/lower livestock numbers.
- Operational context affects the profit-generating activities available to PVUs. For example, the first Khentii PVU and the Sukhbaatar PVU do not heavily utilize drug sales to generate profit because their herders live close to the aimag center where they can buy directly from pharmacies. However, the second Khentii PVU has capitalized on this context by opening a pharmacy that generates considerable profit through drug sales.

Figure 2 | Select PVU Case Studies



# Major Barriers to PVU Growth

## Herder Payment Methods

Herders do not have a regular source of income. Generally, they receive the primary parts of their income twice a year – during cashmere season (May/June) and when they slaughter their livestock (November). This irregularity forces many of them to pay PVUs on credit or in livestock. Credit payments can take herders one to three months to pay off, if they are paid off at all. When livestock are provided they are often over valued against the market rate. This causes PVUs to be unfairly reimbursed for their services. Additionally, depending on the eventual result of herder activities, herders may pay less/not pay for on-credit PVU services e.g. if they have a bad sales year for cashmere.

Herder payment methods limit PVU working capital. PVUs do not receive reimbursement for their services when they administer the services. Additionally, they often receive insufficient reimbursement because of livestock payments or because herders had a bad year in sales.

## Herder Payment Unwillingness

Herders are unwilling to pay for certain PVU services due to historical precedent, the current herder practises, and their personal relationships with PVUs. This unwillingness prompts many herders to pay irregularly for services or not pay at all. Multiple market actors report that even though this attitude is slowly changing, it remains a major issue for PVUs.

- **Historical Precedent:** under the planned economy before 1990, provision of medication and animal healthcare was largely free of cost; hence the majority of herders are unwilling to pay for those services today. Instead, there is an expectation that the government should pay for it.
- **Herder Practises:** large livestock numbers and volume-focused livestock management contributes to an attitude where one or two livestock deaths are not considered a noticeable loss. In this context, the cost of expensive operations to save one animal's life is generally too high given its diminished value in the operational context i.e. calculated revenue benefit of vet assistance is not greater than the cost of assistance.
- **PVU Personal Relationship:** PVUs work in close proximity with the herder households in their soum and are generally friends or relatives with them. This leads to service provision being perceived as a favour, which does not need to be paid for/adequately paid for.

Herder unwillingness to pay limits overall revenue for PVUs by limiting both the activities that can contribute to PVU income and the amount of profit that PVUs can generate. Additionally, it hampers development of PVU services because PVUs are not incentivized to improve services that are not generally paid for. For example, as consultation services are generally provided free of charge, PVUs are dissuaded from improving consultative services which otherwise could provide a robust method for remote veterinary care.

## High Operational Costs

PVUs generally operate with high operating costs for their key activities, limiting their ability to make profit. The specific costs and the manner in which they affect baseline PVU profitability depend a lot on the operational context of the PVU. However, the following patterns have been identified:

- Rural PVUs have high fuel costs because of long distances between rural PVU facilities and herder households and large distances between different herder households. Approximately 80% of PVUs have to travel 100kms or more to reach herder households.
- Urban PVUs, particularly those in UB, have high utilities and rental expenses (unless the PVU owns the property). This high fixed expense has a significant impact on profitability.
- Staffing costs are generally high for PVUs if they are incurred. Many PVUs avoid this charge by enlisting family members as assistants/veterinary paraprofessionals/veterinarians whenever possible to reduce costs. Otherwise PVUs reduce staffing costs by paying staff on an on-call basis as opposed to a regular salary.

## **Vaccination Services Reliance**

Currently the majority of PVUs rely heavily on vaccination services to drive revenue. This is problematic in the long term for a number of reasons including the following:

- PVUs receive income for vaccination services with a delay of one to three months after the PVU delivers and incurs the cost of service. This significantly contributes to a lack of working capital and requires PVUs to take loans or use their own savings to cover the shortfall. Additionally, it puts undue stress on PVUs due to uncertainty around when substantial portions of their revenue will be received.
- Fees received by the government are often less than those budgeted for by the PVU. This makes revenue forecasts and project planning activities difficult, handicapping PVU ability to effectively plan and grow their business.
- The number of administered vaccinations often relies on unpredictable factors such as disease outbreak. This makes revenue forecasts and project planning activities impromptu, handicapping PVU ability to effectively plan and grow their business.
- The regulatory environment concerning vaccination services is shifting towards herders becoming increasingly responsible for vaccination payment, reducing the certainty of payment for PVUs and potentially leading to reductions in the number of vaccinations to be administered.

## **Insufficient Working Capital**

PVUs have insufficient working capital due to a number of issues, including those listed above (high operational costs, herder payment methods, and delays in vaccination services income). This leads PVUs to rely on savings or loans for service continuity. It also affects PVU ability to maintain strong relationships with suppliers, e.g. pharmaceutical importers, due to a lack of working capital to ensure the suppliers are paid consistently on time. Additionally, it renders PVUs unable to make sufficient capital investments to improve their businesses. For example, some PVUs report being unable to purchase the necessary drug sales inventory to allow them to make a volume business of selling them.

## **Limited Business Management Skills**

PVUs generally display limited business management skills in their operations. This is largely due to a focus on the clinical aspects of their operations, the large amount of livestock PVUs are responsible for in rural areas, and the clinically centered structure of the veterinary sciences curriculum at the tertiary level. This results in:

- A lack of strict operational practises e.g. strict payment collection/consistent service charge practices that contributes to the divide between the professional/personal relationship of PVU and herder households being blurred and the revenue of the PVU being affected.
- A lack of business administration activities in PVUs such as financial planning, cost and revenue projection, and income diversification efforts. For example, conducting income diversification activities could assist PVUs in acquiring alternative income streams to deal with seasonal variation in their traditional income streams.

## Key Recommendations

### 1. Increased Drug Sales

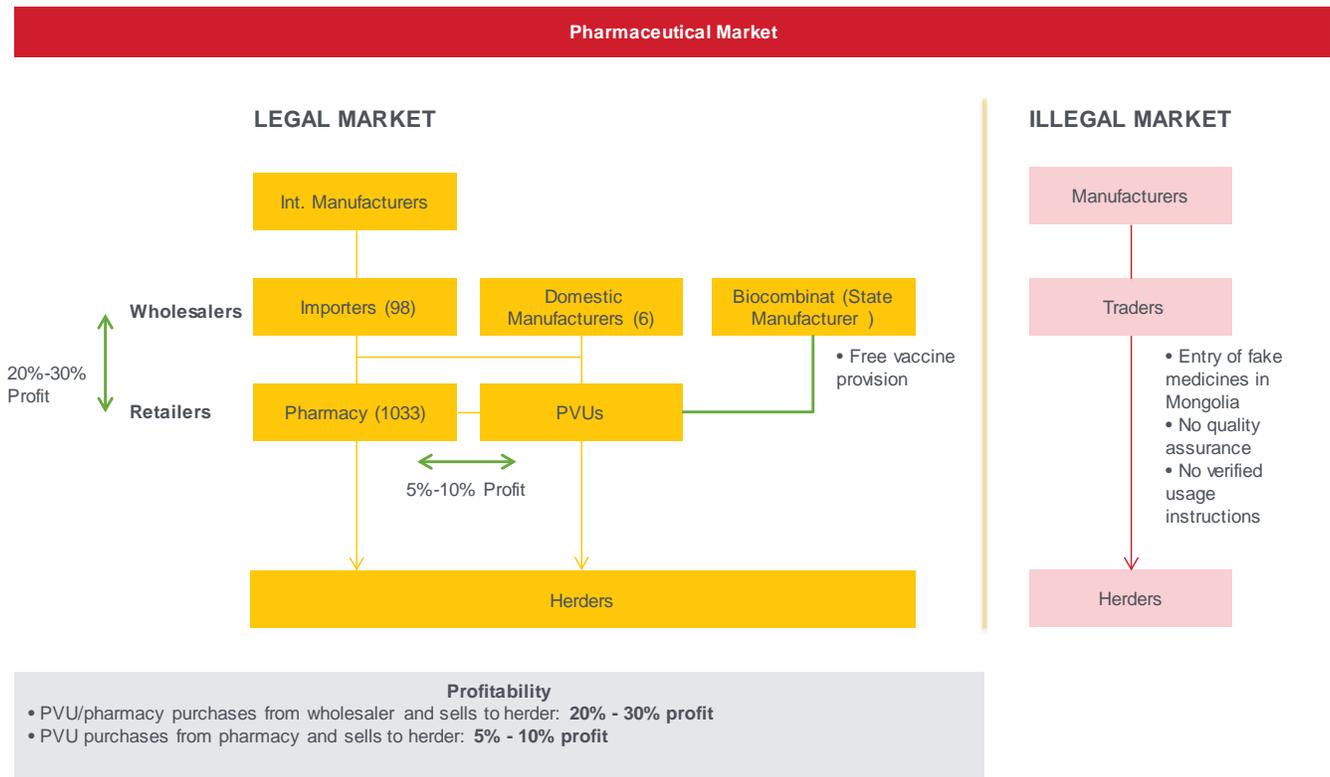
#### Contributing Factors

- PVU access to wholesale drug market lends opportunity for high profit margins on drug sales (20%-30% - see figure 3) that is not affected by the high operational cost issue associated with other PVU income streams.
- PVU sector trends indicate vaccination income will decrease and be offset by an increase in income in other activities including drug sales.
- Prevalence of fake products lends opportunity for differentiation through genuine product provision.
- Lack of herder drug knowledge lends opportunity for differentiation through proactive product education efforts.
- Increased responsibility for animal healthcare by herders will drive changing herder attitudes on utilising veterinary medicine.

#### Key Constraints

- Insufficient working capital affects PVU ability to maintain strong supplier relationships, build sufficient drug sales inventory, and build/expand drug sales operation e.g. pharmacy expansion.
- Herder unwillingness to pay pushes herders to buy the cheapest fake drug products and not purchase more expensive genuine products from PVUs. Lack of herder drug knowledge contributes to this constraint.
- Some herders may want to purchase/administer drugs themselves; this is more prevalent in areas where urban centres are within easy reach and/or where herders have ready access to fake medicine traders or markets.
- Limited business management skills in PVU operations makes it difficult for PVUs to execute appropriate business planning activities to set up an effective drug sale business e.g. identifying optimal suppliers. Additionally, it affects PVU ability to conduct on-going management activities e.g. supplier management.

Figure 3 | Pharmaceutical Market Summary



## Recommended Actions

**Maintain and leverage supplier relationships:** PVUs should develop strategies to locate suitable suppliers, with an importer focus whenever possible, and with an emphasis on effectively managing and leveraging the relationship in the long term.

**Provision of clear instructions on drug use and genuine product advocacy:** PVUs should ensure customers are purchasing the correct product for their issue, provide the appropriate information upon sale, and follow-up to ensure product was used appropriately. Additionally, PVUs should routinely perform advocacy for genuine products including education of residue and health-outcome benefits.

**Proactive operational development:** PVUs should ensure that their drug sale operation is given appropriate development focus as an operation with its own set of specific activities e.g. proactive pharmaceutical product promotion and analysing customer demand across a range of pharmaceutical products.

## Overprescription Issue

Overprescribing of medication is not encouraged in the interest of sales. Higher sales should occur through responsible provision of medication. Prevention is a combination of good practise in animal nutrition, animal handling and vaccination provision. Treatment is secondary to prevention.

## 2. Increased Consultations

### Contributing Factors

- PVUs currently have strong consultation skills due to the volume of free consultation currently provided and the diverse range of livestock they provide veterinary consultation for.
- PVU sector trends indicate vaccination income will decrease and be offset by an increase in income in other activities including veterinary consultation. Additionally, veterinary consultation has been identified as a service to become in trend over the mid to long-term.
- Prescription requirements for herders under the new Animal Health Law and the lack of herder drug knowledge will drive herders to consult more with PVUs when using veterinary drugs.
- Increased responsibility for animal healthcare by herders will drive changing herder attitudes on paying for veterinary expertise.
- High operational costs associated with conducting household visits make mobile consultation (consultation via mobile phone) desirable given its significantly lower operational costs.

### Key Constraints

- Herder unwillingness to pay drives them not to value PVU consultation services in urban and rural contexts. In both contexts, this lack of value leads to herders not paying for consultation services.
- Herder lack of drug knowledge drives them not to see the need for consultation when purchasing and administering drugs.
- Limited business management skills in PVU operations makes charging for consultation more difficult especially when PVUs have personal relationships with herders.
- Aimag level service reference costs for consultation services limit PVU ability to set a fair consultation price.

#### Free Consultation Issue

PVUs spend an average of 2-3 hours every day providing free consultation to herders. This can take the form of questions asked in a social setting or the herder calling his PVU with questions. This makes consultation work constitute a significant daily portion of work for PVUs.

### Recommended Actions

**Implementing a consultation charge:** PVUs should begin the process of transitioning to a charged consultation model. The transition should be staged slowly, beginning with embedding consultation charges in other services then with gradual acceptance implementing a standalone charge.

**Deliver high quality consultations:** PVUs should increase consultation quality through provision of sufficient clinical and pharmaceutical information so that herders can utilise the consultation to confidently implement the appropriate means of care for their livestock independently.

**Increased focus on consultation as a mean of care:** PVUs should gradually increase their availability for consultation and promote the positive health outcomes of regular consultations.

## 3. Improved Business Management Skills

### Contributing Factors

- Increased government pressure on quality of PVU activities e.g. current increased demand for robust disease prevalence reporting, will put pressure on PVUs to adapt more professional and sophisticated operations.
- Reduction in government vaccine ownership will shift payment responsibility of certain vaccines to herders and will make them more active consumers that will demand more from their PVUs.
- Increased responsibility for animal healthcare by herders will drive changing herder attitudes towards their PVUs.
- Addresses insufficient working capital issues by building business administration capacity and focusing on implementing stricter operational practices e.g. a strict credit collection policy.

### Key Constraints

- The informal relationship between PVUs and herders makes it difficult for PVUs to enforce a more professional relationship between them.
- Herder payment methods and herder payment unwillingness makes enforcing stricter operational policies difficult e.g. enforcing a strict non-cash payments policy.
- Currently, veterinarians get minimal business administration training throughout their university study with focus put on clinical aspects of running a PVU as opposed to the business/operational aspects.

### Recommended Actions

**Stricter credit payments policy:** PVUs should begin formalising their service on credit practises. This would involve setting repayment periods with associated charges and implementing a system of follow-up to ensure payment receipt

**Stricter non-cash payments policy:** PVUs should begin formalizing their service on non-cash payment practices. This could involve setting limits on how much of a service fee can be paid through non-cash means and/or establishing incentives for cash payments e.g. giving higher service costs for non-cash payments.

**Focus on improving business administration activities:** PVUs should recognise the need to improve their business administration activities. Key activities to improve include business planning, project planning, and cost/revenue accounting. Improvements should be driven by personal learning through online and physical resources and PVUs attending training courses where possible.

#### Scope of Business Management Recommendations

Recommended actions cover the business management areas that are in need of the most action. The implementation process of the recommendations is iterative. PVUs should constantly look at ways to implement new policies and procedures that assist their business growth and profitability.

# Conclusion

A large portion of the barriers limiting PVU profitability stem from a culture where herders still do not recognize the need to pay substantially for animal healthcare services. This creates an inherent barrier to a successful PVU operation as currently the government is the primary source of income for PVUs, a remnant of the pre-1990 planned economy. In a market economy the herders should be the primary consumer of PVU services not the government. Improving PVU profitability in the future requires recognizing this fundamental relationship, both from PVUs and herders.

This report contains a series of recommendations identified as potential ways that PVUs can recognize their position as veterinary small businesses and start to increase their profitability. By developing their business management skills, PVUs can begin separating more clearly the line between their professional relationship with customers and their personal relationship with them. By diversifying and attempting to build more commercially based income streams such as pharmaceutical sales PVUs can address the homogeneity of their current income sources. By addressing structural issues such as the lack of value attributed to valuable consultation services PVUs will work towards improving their profitability in the mid to long term.

PVUs represent a key factor for the future success of the Mongolian animal health sector. The feasibility and profitability of their operations is a key indicator of their growth potential and the results of this report can guide future efforts to realize that potential.

# Appendix – PVU Case Studies

## Rural PVU Case Studies

Figure A1 | Rural PVU Case Studies

Töv PVU	Selenge PVU	Khentii (1) PVU	Khentii (2) PVU (inc. pharmacy)	Sükhbaatar PVU
<p>REVENUE (10,000,000₮)            Vaccinations (70%): 7,000,000₮            Drug Sales (5%): 500,000₮            Clinical Services (20%): 2,000,000₮            Origin Certificates (5%): 500,000₮</p>	<p>REVENUE (11,000,000₮)            Vaccinations (73%): 8,000,000₮            Drug Sales (10%): 1,100,000₮            Clinical Services (14%): 1,500,000₮            Origin Certificates (3%): 400,000₮</p>	<p>REVENUE (70,000,000₮)            Vaccinations (90%): 63,000,000₮            Drug Sales (0%): 0₮            Clinical Services (3%): 2,000,000₮            Origin Certificates (7%): 5,000,000₮</p>	<p>REVENUE (112,000,000₮)            Vaccinations (9%): 10,000,000₮            Drug Sales (89%): 100,000,000₮ (pharmacy)            Clinical Services (0%): 0₮            Origin Certificates (1%): 2,000,000₮</p>	<p>REVENUE (40,000,000₮)            Vaccinations (75%): 30,000,000₮            Drug Sales (2%): 1,000,000₮            Clinical Services (18%): 7,000,000₮            Origin Certificates (5%): 2,000,000₮</p>
<p>DETAIL</p> <p><b>Location:</b> en-route to UB  <b>Livestock:</b> 32,500  <b>Vaccination Profit:</b> N/A  <b>Credit Payment:</b> 30% of herder payments  <b>Livestock Payment:</b> N/A  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Herder inconsistent payment &amp; non-payment</li> <li>• Delay in vaccine payment &amp; herder debt payments</li> <li>• In 2017 enforced rule to refuse livestock as payment due to overvaluation</li> </ul>	<p>DETAIL</p> <p><b>Location:</b> rural  <b>Livestock:</b> 43,000  <b>Vaccination Profit:</b> N/A  <b>Credit Payment:</b> 60% of herder payments  <b>Livestock Payment:</b> N/A  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Herder inconsistent payment &amp; non-payment</li> <li>• Delay in vaccine payment &amp; herder debt payments</li> <li>• Lack of working capital to purchase sufficient drug sale inventory</li> </ul>	<p>DETAIL</p> <p><b>Location:</b> close to aimag centre  <b>Livestock:</b> 299,000  <b>Vaccination Profit:</b> 10m (16%)  <b>Credit Payment:</b> 10% of herder payments  <b>Livestock Payment:</b> 30% of herder payments  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Delay in vaccine payment leads to loan to cover shortfall</li> <li>• Lack of working capital limits expansion project</li> <li>• Herder inconsistent payment &amp; non-payment</li> </ul>	<p>DETAIL</p> <p><b>Location:</b> close to aimag centre  <b>Livestock:</b> 18,000  <b>Vaccination Profit:</b> 6m (60%)  <b>Credit Payment:</b> 20% of herder payments  <b>Livestock Payment:</b> 5% of herder payments  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Herder inconsistent payment &amp; non-payment</li> </ul>	<p>DETAIL</p> <p><b>Location:</b> close to aimag centre  <b>Livestock:</b> 100,000  <b>Vaccination Profit:</b> 6m (30%)  <b>Credit Payment:</b> 10% of herder payments  <b>Livestock Payment:</b> 30% of herder payments  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Delay in vaccine payment leads to loan to cover shortfall</li> <li>• Lack of working capital limits expansion project</li> <li>• Herder inconsistent payment &amp; non-payment</li> </ul>

Figure A2 | Rural PVU Activity Profitability

<p><b>Drug Sale Profitability</b></p> <p>Depends on source:</p> <ul style="list-style-type: none"> <li>• Sourced from importers: 20-30% profit</li> <li>• Sourced from pharmacies: 5-10% profit</li> </ul> <p>Issues:</p> <ul style="list-style-type: none"> <li>• Herders prefer fake because cheaper</li> <li>• Need to educate about residue/health issue</li> </ul>	<p><b>Clinical Services Profitability</b></p> <p>Depends on service:</p> <ul style="list-style-type: none"> <li>• Anti-parasitic treatment: depends on micro factors (i.e. herder distribution/service reference costs)</li> <li>• Expensive services (i.e. surgeries) herders don't pay</li> <li>• Livestock dipping is very profitable (&gt;50%) but equipment and staff costs high</li> </ul>
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Approximate Figures

# UB PVU Case Studies

Figure A3 | Urban PVU Case Studies

UB (1) PVU	UB (2) PVU
<p>REVENUE (26,700,000₮)</p> <p>Vaccinations (49%): 13,000,000₮</p> <p>Drug Sales (1%): 250,000₮</p> <p>Clinical Services (10%): 2,550,000₮</p> <p>Origin Certificates (40%): 10,900,000₮</p>	<p>REVENUE (60,000,000₮)</p> <p>Vaccinations (50%): 30,000,000₮</p> <p>Drug Sales (10%): 6,000,000₮</p> <p>Clinical Services &amp; Origin Certificates (40%): 24,000,000₮</p>
<p>DETAIL</p> <p><b>Vaccination Profit:</b> N/A  <b>Credit Payment:</b> N/A  <b>Livestock Payment:</b> N/A  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Delay in vaccine payment</li> <li>• Utilities is a major cost driver</li> <li>• Lack of working capital delays improvement projects significantly (e.g. 3yr refurbishment)</li> </ul>	<p>DETAIL</p> <p><b>Vaccination Profit:</b> N/A  <b>Credit Payment:</b> 10% of herder payments  <b>Livestock Payment:</b> 30% of herder payments  <b>Major Issues:</b></p> <ul style="list-style-type: none"> <li>• Delay in vaccine payment leads to loan to cover shortfall</li> <li>• Lack of working capital limits expansion project</li> <li>• Herder inconsistent payment &amp; non-payment</li> </ul>

## CONTACT

SWAPNIL MINDHE

Market Systems Analyst | Mercy Corps Mongolia

[smindhe@mercycorps.org](mailto:smindhe@mercycorps.org)

ENKHTSETSEG GANBOLD

Director of Programs | Mercy Corps Mongolia

[enkhtsetsegg@mercycorps.org](mailto:enkhtsetsegg@mercycorps.org)

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45 SW Ankeny Street  
Portland, Oregon 97204  
888.842.0842  
[mercycorps.org](http://mercycorps.org)