



Hutchins Center
on Fiscal & Monetary Policy
at BROOKINGS



Center for
Health Policy
at BROOKINGS

Reining in Prescription Drug Prices

May 2, 2017



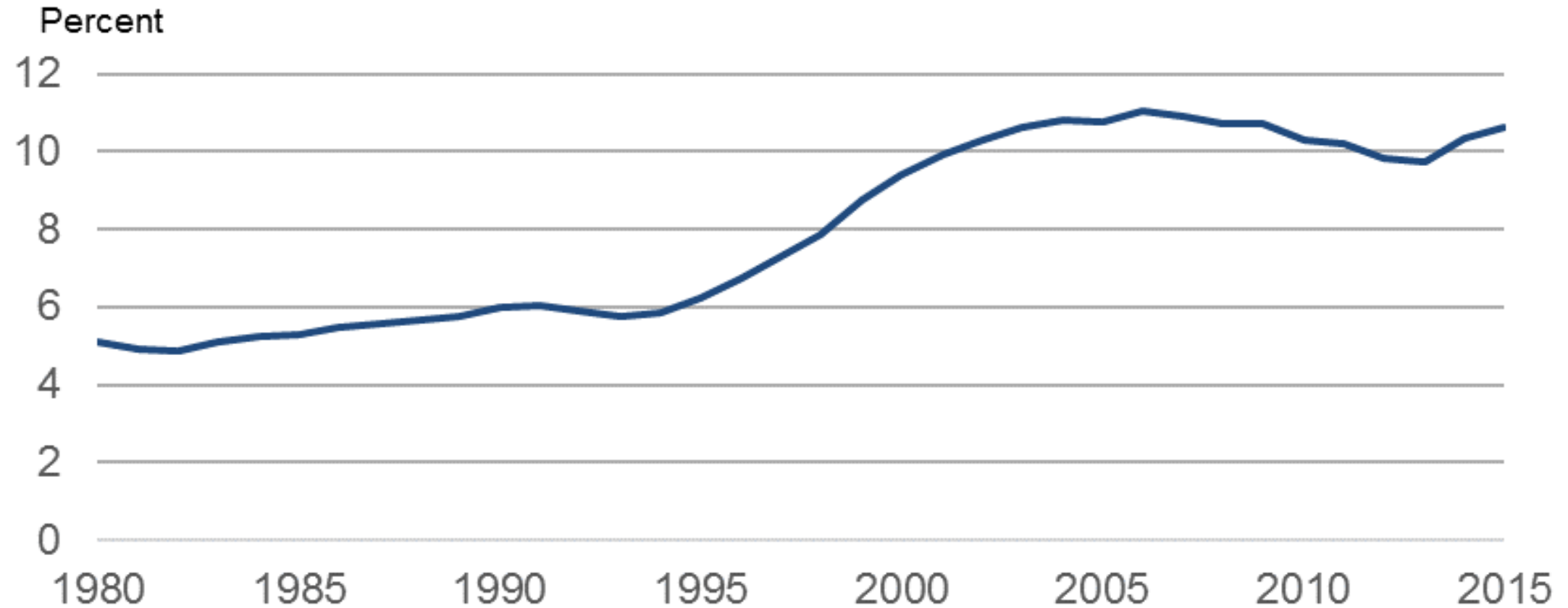
Drug Spending in the United States

- Retail drug spending \$325 billion in 2015.
- About \$1,000 per person.
- About 10% of total health spending.
- An additional \$125 billion on drugs administered in hospitals or physician offices.



Prescription drugs increasingly important component of health spending

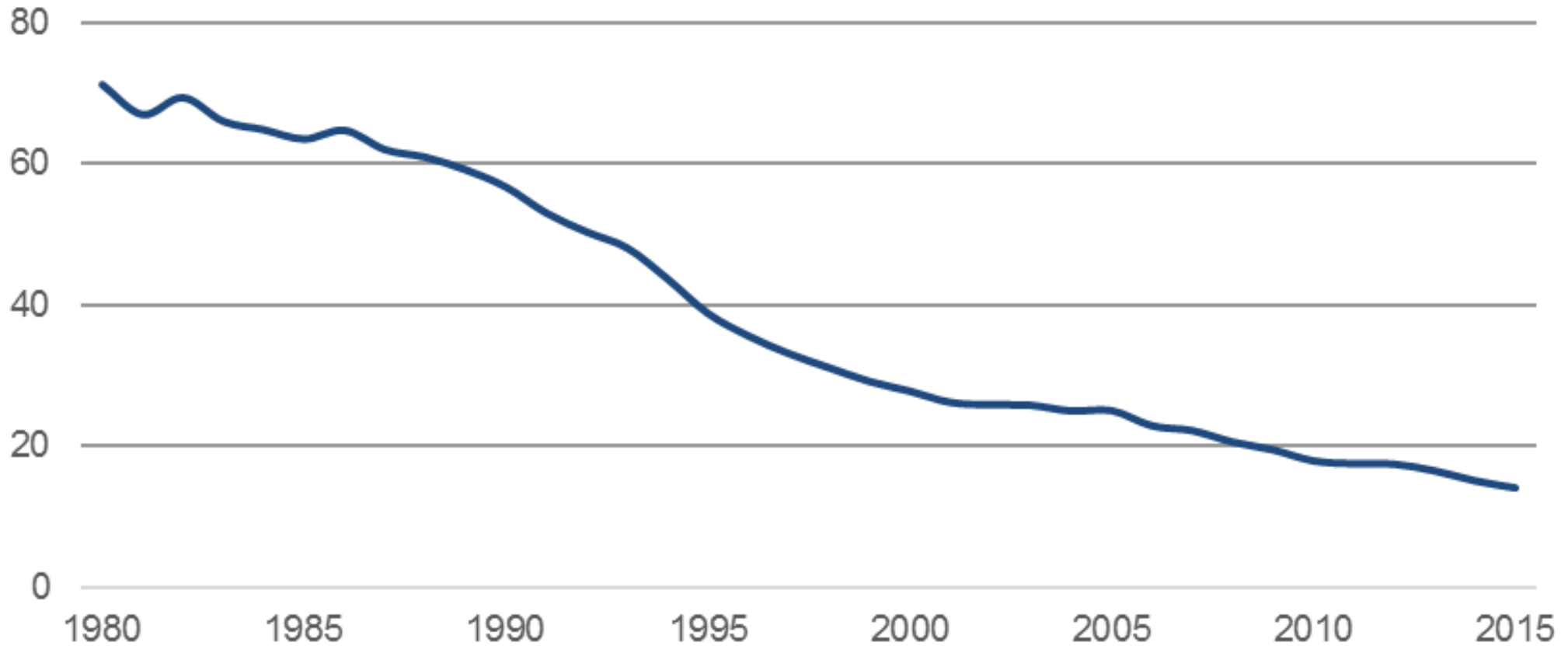
Retail prescription drug spending share of health spending



Consumers increasingly insulated from drug prices at point of purchase

Drug spending out-of-pocket share

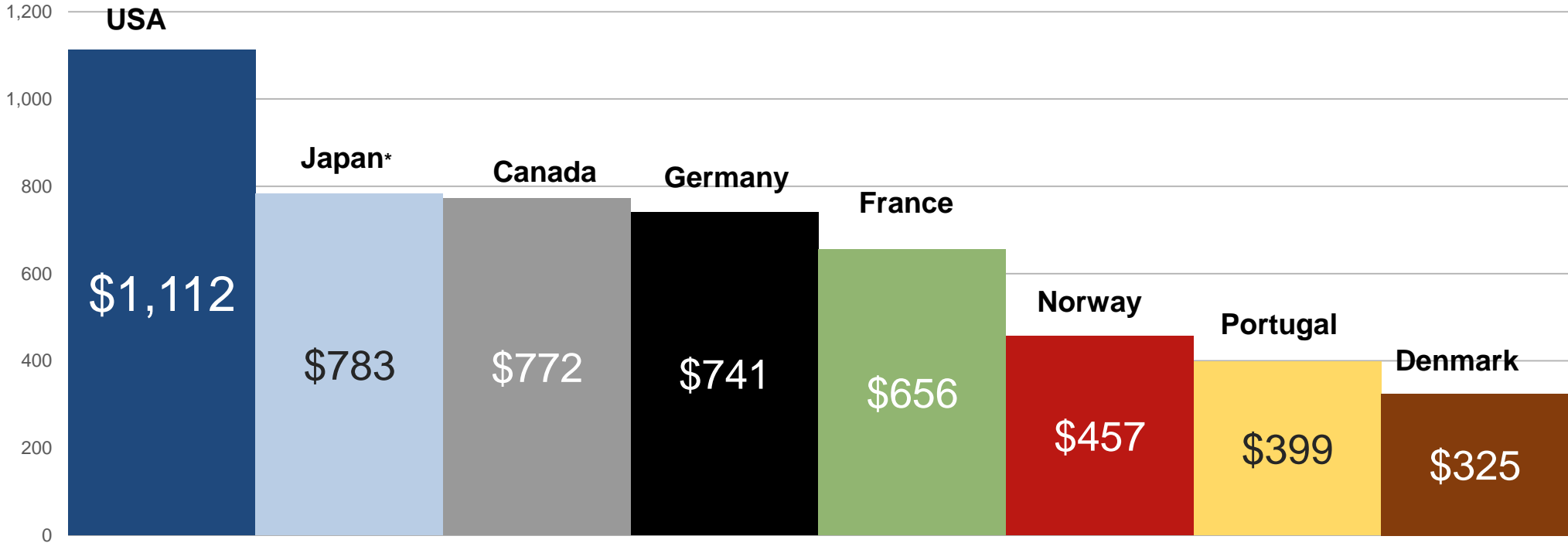
Percent



Per person spending is much higher in the U.S. than elsewhere

Per Capita Retail Drug Spending in 2014, by Country

\$US Dollars



Basic Economics of Drug Development

- Large fixed costs to invent and test new drugs.
- Huge uncertainty about likely returns to R&D.
- Small marginal costs to produce.
- Without regulation, no one would want to invest in pharmaceutical R&D, because another firm could copy technology and undercut.



Regulation gives market power to drug companies

- Patents – last 20 years from date of filing.
- FDA provides “exclusive marketing rights” once they have approved a drug
- Length of exclusive marketing rights depend on type of drug, with drugs with small markets (“orphan drugs”) given longer rights so as to encourage innovation.
- After both patent and exclusive rights expire, generics can enter the market
- On average, brand-name drugs have 13 or so years of sales before a generic competitor enters the market



Tradeoffs: Incentives for Innovation, Access, and Fairness

- Higher-than-normal profits and prices greater than marginal cost essential to encouraging innovation
- But high prices limit access to drugs: increase out-of-pocket costs and insurance premiums
- High prices make generous insurance necessary, but insurance also leads to too little price sensitivity on the part of consumers
- And monopoly power may allow drug companies to reap too much of the benefits of new drugs.



What can be done?

- Increasing desire to take steps to rein in drug prices. Question is how to do that without unduly harming innovation.
- All three of this morning's proposals recognize the need for drug companies to retain significant pricing power and recognized the large benefits we get from drug development.
- But they suggest changes in areas where drug company market power seems larger than can be justified.
- Papers all available at www.brookings.edu/hutchinscenter

