American Enterprise Institute for Public Policy Research

Media inquiries: Véronique Rodman
202.862.4870 (vrodman@aei.org)
Orders: 800.462.6420 or www.aei.org/books

The AEI Press

Government Price Controls on Drugs Will Reduce Innovation and Cost Lives

New Book Shows Even Comparative Effectiveness Proposals Will Hamper New Drug Development

FOR IMMEDIATE RELEASE: December 17, 2008

Breakthrough drugs have saved millions of lives and improved the health of countless people around the world. Unfortunately, they are also expensive, leading many U.S. political leaders to call for price controls, importation, or other procedures to reduce their cost.

In *Pharmaceutical Price Regulation: Public Perceptions, Economic Realities, and Empirical Evidence* (AEI Press, January 2009), economists John A. Vernon and Joseph H. Golec argue that price controls and other cost-limiting measures will starve pharmaceutical companies of the R&D money required to develop new drugs. A drug can cost $1 billion or more before it ever appears in the marketplace—and only three out of every ten new drugs ever recoup their development costs. This groundbreaking monograph demonstrates empirically how the free-market system of drug pricing is vital to the continuing flow of breakthrough drugs.

- Europe's tight control over drug spending has led to sharp restraints on drug R&D spending. Between 1986 and 2004, Europe's pharmaceutical industry R&D grew at merely one-half the rate of that in the United States. In the mid 1980s, Europe's drug R&D exceeded that of the United States by 24 percent. By 2004, however, it trailed U.S. spending by 15 percent.

- America's mere flirtation with heavy government price controls—the Clinton health plan of 1993—took an almost devastating toll on the very companies that conduct the most intensive R&D into new drugs. Vernon and Golec's research shows that in the aftermath of the plan's announcement, the more intensely R&D–focused a company was, the more its stocks dropped. Small biotechnology firms' stock prices fell the most and recovered only slowly.

- Vernon and Golec argue that allowing drug importation is a frontal assault on the future of pharmaceutical industry R&D. Importation undermines drug companies' efforts to charge different prices in different markets, leading to a single worldwide price—one that is simultaneously too high for many poorer countries and too low for the drug companies to recoup their upfront R&D investments.

The authors show that drug companies take a long-term view towards R&D investment, balancing projected profits against the costs of clinical development. This puts them in conflict with politicians, who tend to focus on the short-term concerns of current voters. As a result, prices set in the political arena will reflect current voters' wishes, as opposed to the full economic value that pharmaceuticals would attain in a free price market. With less money to invest in R&D, drug companies have no choice but to curtail development that would serve the interest of future generations.

Vernon and Golec warn that while the United States has largely avoided the heavy-handed role of government price controls, efforts by Congress and influential policymakers are setting the country on precisely this course. "Pharmaceutical price controls," they argue, "constitute a short-sighted, wrong-headed, and possibly dangerous policy. The prices set by the free market are the signals absolutely necessary for corporations to decide whether to undertake expensive, risky research into new drugs."

John A. Vernon is a professor in the Department of Health Policy and Management at the University of North Carolina at Chapel Hill, where he also holds appointments in the Kenan-Flagler Business School and the UNC School of Pharmacy. He is also a faculty research fellow with the National Bureau of Economic Research and the former senior economic policy adviser to the Office of the Commissioner at the U.S. Food and Drug Administration.

Joseph Golec is an associate professor of finance at the University of Connecticut.

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PHARMACEUTICAL PRICE REGULATION:
PUBLIC PERCEPTIONS, ECONOMIC REALITIES, AND EMPIRICAL EVIDENCE

John A. Vernon and Joseph H. Golec

978-0-8447-4277-9 • Paper • $15.00 • 83 pages • January 2009