

Pharmaceutical Price Controls Destroy Innovation and Harm Patients

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The IQVIA Institute (2021) forecasts total medical spending in the U.S. will reach between \$380-\$400 billion by 2025. A growing component of this jarring figure is prescription drug costs. Nearly 48 percent of Americans use at least one prescription drug daily (CDC, 2019). More people might use prescription drugs if they could afford them. A 2019 survey finds nearly 30 percent of prescriptions remain unfilled because patients fear they will be too expensive (KFF, 2020).

Skyrocketing drug prices have motivated politicians to step in. Price controls are their latest (of many failed) attempts to make drugs cheaper. Although price controls for drugs were once political rhetoric, they might soon become the next foolhardy attempt to fix healthcare woes. Colorado recently became the first state to implement a price cap on insulin (Zialcita, 2021). Now North Dakota is considering a similar policy. N.D. Senate Bill No. 2170 aims to fine drug producers \$1,000 for charging higher prices than Canadian pharmacies.

North Dakota does have a prescription drug price problem. In 2019, North Dakotans spent nearly \$1.5 billion on prescription drugs (Definitive Healthcare, 2022). This ranks amongst the highest per capita expenditures in the country. But price controls are no solution. At best, they fail. At worst, they create severe unintended consequences which harm consumers and producers.

Price controls for pharmaceuticals are a clear example of the dangers of well-intended but poorly thought out policy—crippling suppliers from innovating new and cheaper products while slashing patient access to much-needed (even life-prolonging) medical goods. North Dakota's characteristics and economic conditions would only make these consequences worse.

Price Controls: Bad in Theory, Worse in Practice

Prices play an indispensable role in the economy. They inform both buyers and sellers how much of a good is available. Higher prices motivate producers to find profitable ways to make more. They also encourage consumers to buy less (or buy something else).

When policies prevent prices from rising, consumers buy more while producers make less (or make something else). Price controls on prescription drugs reduce availability and limit the incentive to develop new products (Calfee, 2001). Both parties are worse off—the worst outcome a policy can create.

This fundamental economic lesson applies to all products in all markets. Shuttenger (2014) reviews the use and effects of price controls extending back thousands of years and for hundreds of products. The results are always the same: less availability and rippling effects across other markets worsen an already difficult situation.

Numerous studies demonstrate that prescription drug prices, even when high, are no exception to this predictable pattern. Klye and Schulthess (2007) and Bowen (2021) find drug developers were less likely to dedicate funds to R&D and introduce new drugs in countries with pharmaceutical price controls. Eger and Mahlich (2014) similarly find that firms selling drugs in price-regulated European markets have lower R&D spending. Philipson and Durie (2021) review the Lower Drug Costs Now Act proposed by the Biden Administration and estimate the act would cost between 167-342 new drug approvals while reducing R&D spending by about \$952.2 billion-\$2 trillion across eight years.

Cutting R&D comes at the cost of future innovation—meaning fewer pioneering medical discoveries, cheaper drugs, and lifesaving medications. Motkuri and Mishra (2018) find that India’s efforts to implement price controls considerably reduced patient access to lifesaving drugs. In their illustrative but concerning paper titled *The Cost of U.S. Pharmaceutical Price Reductions: A Financial Simulation Model of R&D Decisions*, Abbot and Vernon (2005) note that even modest price controls in the U.S. pharmaceutical market could truncate R&D expenditures by five percent. For reference, federal funding provided to Pfizer to produce the first authorized Covid-19 vaccine was only an eight percent R&D increase.

Decreased profitability will also sharply reduce current drug availability (Ingram 2011). Although some “blockbuster” drugs have high-profit margins, most prescription drugs make modest gains. Abbot and Vernon (2005) note that only 30 percent of drugs recoup their R&D expenditures once they reach U.S. patients.

Drug shortages caused by price controls are well-documented. Slin (2007) chronicles a decade of drug shortages in the United Kingdom during the 1950-1960s following attempts to make drugs cheaper using price controls. Even price controls on more lucrative drugs fail to deliver on their goals.

In 2019, Colorado became the first state to cap insulin co-pays to \$100 per month. Nearly a year later, a survey found 40 percent of Coloradan diabetics still rationed their insulin because of a lack of availability (March, 2021). North Dakota and Minnesota residents frequently travel to Canada (which also uses price controls) to buy cheaper insulin (Davie, 2019). Consequently, Canadian pharmacies often restrict how many vials of insulin patients can purchase at a time, leaving Canadians with less access (Mueller, 2017).

What Prescription Drug Price Controls Would Mean for North Dakotans

Healthcare’s complex network of insurance providers, employers, third-party agencies, and medical professionals means the harmful effects of price controls extend well beyond patients and drug producers. Price controls and ill effects cast a wide and devastating net in a state with predominantly rural health like North Dakota.

When drug producers lose profitability, they produce fewer drugs with lower profit margins. Consequently, cheaper drugs become harder to find and other drugs get prescribed for their secondary effects. Changing pharmaceutical prices also requires PBMs, PSAOs, and similar organizations to renegotiate drug prices with pharmacies and insurance providers. The outcome is cost-shifting strategies that place further financial burdens on the drug providers (including wholesalers) and patients to cover the costs of drugs that remain on the market.

With nearly 40 percent of North Dakotans living in a rural area, higher insurance premiums and lower coverage put many farther away from accessing pharmaceuticals (N.D. Chamber of Commerce, 2021). This is especially harmful as rural populations frequently have higher rates of diabetes and other chronic health conditions (Smith, Humphries, and Wilson, 2008). Rising premiums also increase financial difficulties for the nine percent of North Dakotans without any health insurance coverage (KFF, 2020).

Less access to drugs is particularly concerning in North Dakota. Although North Dakota is one of the least populated states, it ranks 20th in the number of prescription drugs filled and 11th in the number of unique prescriptions filled annually. These figures indicate North Dakota patients need diverse and frequent pharmaceutical access (Definitive Healthcare, 2022).

Pharmaceutical price controls also harm small businesses. Nearly 60 percent of U.S. employees receive some health insurance from work, making employers one of the largest health insurance providers. When the cost of providing health insurance to employees rises, so does the cost of retaining and hiring new employees, leading to fewer jobs. Baicker and Chandra (2005) estimate a 10 percent increase in health insurance premiums results in one fewer hour worked per week with a two percent lower chance of being hired (health insurance premiums have risen 50 percent since 2000).

As categorized by the Small Business Administration, nearly 98 percent of businesses incorporated in North Dakota are small businesses (Boland, 2021). Combined with a persistent state-wide labor shortage (O'Day, 2021), the secondary effects of pharmaceutical price controls would likely have a considerable negative impact.

Conclusion

Higher prices for vital goods like prescription drugs have falsely led many to call on price controls to make them cheaper. While well-intended, price controls only attempt to limit price increases. Their actual effect is to limit innovation and access. Thousands of examples and a large body of research consistently find price controls fail to deliver while causing considerable harm. Implementing them in North Dakota would be a disastrous misdiagnosis.

Citations available upon request.

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