

Contributed by Merrill Matthews Jr., Ph.D.

# ANSWERING THE INDUSTRY'S CRITICISMS: PRICES AND PROFITS

**F**or several years, the pharmaceutical industry has been under attack by people and organizations claiming to want nothing more than to ensure people have access to affordable medicines. Although most of the criticisms of the industry are wrong and even disingenuous, their concerns must be answered and put in the context of other industries and well-accepted business practices.

## CRITICISM NO. 1: The pharmaceutical industry is the most profitable in the country.

In *Fortune* magazine's annual ranking of the top 500 companies, the 14 companies that make up the "pharmaceuticals" category had a median profit (as a percent of revenue) of 18% in 2001 — more than any other industry median. The most profitable drug company on the list was Amgen at 28%. But Pharmacia and Abbott both reached only 7% profit, and Genzyme recorded a 9% loss. On the other hand, Coca-Cola had a 20% profit, Bank of New York recorded a 19% profit, and Mellon Financial had a profit of 33% (more than any drug company). Microsoft hit 29%, Oracle 24%, SBC Communications earned 16%, and AT&T made 13%. Gannett (publisher of *USA Today*) recorded 13%, while Knight-Ridder reached 15%. Even the *Washington Post* boasted a 10% profit, as much or more than four of the drug companies on the list.

Yes, most "innovator" drug companies make above-average profits. But any economist knows that the riskier the business the higher the profits must be to induce entrepreneurs to take that risk. Creating new drugs is one of the riskiest businesses, with only about one out of 5,000 new chemical compounds making it to market and only three of 10 new approved drugs actually meeting or exceeding their research and development costs.

## CRITICISM NO. 2: Drug prices are high because pharmaceutical companies pay their CEOs outrageously high salaries.

While many of the drug companies pay their CEOs well, those salaries are not out of line with other companies their size. Indeed, they may be on the low side. Last April, *USA Today* ranked total "compensation packages for 103 CEOs at 100 top companies," including the "potential value of stock option grants." And guess what? Many CEOs from other businesses did much better than drug company executives.

Oracle was ranked first because the CEO's salary with add-ons and potential stock options brought his total compensation to \$706 million last year. Cisco Systems and SBC Communications

ranked second and third, respectively. IBM ranked fifth. Even the CEO of Coca-Cola came in ninth with \$100 million — 30% more than the highest-paid drug company CEO. And yet Pfizer's CEO came in at 15 on *USA Today's* chart, even though Pfizer is the fifth largest company in the world, according to the *Wall Street Journal*. Abbott Laboratories' CEO ranked 23, Schering-Plough's CEO was 51, Eli Lilly's CEO was ranked 55, and Johnson & Johnson's CEO was ranked No. 88, even though J&J is the 15th largest company in the world.

But why stop with corporate CEOs? According to *Parade* magazine, TV newswoman Diane Sawyer made \$10 million last year; actress Jennifer Lopez took in \$14.4 million, and Singer Brittany Spears raked in \$38.5 million. Baseball player Mike Piazza got \$15 million, basketball great Shaquille O'Neal received \$29 million, and ex-con Mike Tyson brought in an astounding \$48 million. And none of these "stars" employ 100,000 people all over the world. Where's the outrage over these exorbitant incomes?

## CRITICISM NO. 3: Drug companies are "profiting from pain."

Actually, drug companies profit from the relief of pain and suffering. People must have food on a daily basis, yet no one says that farmers and grocers are profiting from starvation. When people travel, they usually need a place to stay at night. Fortunately, there is a system of hotels and motels across the country ready to meet the travelers' needs. But no one seriously claims that hotels are profiting from homelessness. To the contrary, travelers who need a place to stay are thankful the hotel industry provides lots of options on price, quality, service, and convenience.

Like food and hotels, the drug industry makes a product that many people want and need. Unlike those industries, the innovator drug companies take enormous financial risks. That most drug companies manage to earn a profit, especially in troubled economic times, should elicit praise, not criticism.

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