The global pharmaceutical industry economics essay

Economics

Being one of the biggest players in human welfare, the Global Pharmaceutical Industry is amongst one of the biggest industries but at the same time faces many challenges. This essay will present a full external analysis using various frameworks. PESTEL FrameworkThis framework helps an industry to analyze the macro environmental factors that an industry faces and takes into consideration. Political Factors: There were severe government regulations imposed due to the Thalidomide tragedy that occurred alerting for tighter controls. The government introduced price/reimbursement controls that could not be changed by the supplier since it lacked all the public/political support needed. Delays occurred due to this. In the supply side of the market, to get the approval of the pricing/reimbursement usually takes an year, and in the demand side of the market, institutions such as NICE that make up decisions in cost effectiveness, holdup market penetration. Economic Factors: European free trade movements allowed high penetration into markets with low costs. Growth of the industry is aligned to the GDP growth of a company. The USA was a leading market by a volume and value of $250bn in 2005. International harmonization allowed a faster approval of regulatory procedures via a centralized approach which granted permission to all the member states simultaneously but also brought along risks as a lot was riding at stake on one decision only. Social and Cultural Factors: Ageing populations created intense pressure on healthcare systems (over 65s), being too expensive. Once awareness was created about health, wealthy consumers were ready to buy branded drugs, but those who could not afford them chose generic drugs. Technological FactorsHighly risky, lengthy and

costly R&D process. The use of the internet introduced the allowance of online purchases on a global scale with a faster reach to a larger customer base. Environmental/ Ecological FactorsThere are increasing standards and regulations for environmental protection because of industry operations. Legal FactorsPatent protection was set to 20 years from permanent periods. Prices are no longer set by completion laws, but by governments due to the introduction of parallel trade. Earlier decision making was in the hands of all the medical practitioners since the buyers had little knowledge over these matters, but changed overtime. Copy products were traditionally an issue but intellectual reforms were starting to take place. There is careful regulatory inspection which is governed by legislation. Porter's Five Force ModelThis model helps in determining the strategic position of a firm. C: UsersHPDesktopporter-five-forces-model-of-strategy-480wide. jpgPorter, 1980Threat of Substitute Products. There are a few but competitive substitutes in the market. The availability of cheaper generics drugs with the same active ingredients as the branded drugs poses a high threat. Allegra lost 84 per cent of U. S sales in just 12 weeks after expiry of the patent. The improved computer and chemistry generations (for example, the biotechnology startups) greatly reduced the time frames for ' me-too' drugs to penetrate the market. Following the Thalidomide tragedy, consumers are more suspicious to the drugs being produced and often go for other alternative remedies. A company that may decide to diversify its branded products to generics will increase its market share but not its profits! Bargaining Power of Buyers. Earlier in the 1960s, the decision making was in the hands of the medical practitioners as the final consumers had little

knowledge. As a result, prices were set at insensitive rates. But as we read in the case, the over 65s were the main consumers of the ethical drugs who found the drugs expensive. Demand for the product was high although there is a challenge to meet it. Governments, who are the largest buyers, imposed control prices that controlled the high health expenditures that kept in check some of the huge profits being made. Distributors who act as middlemen tend to buy the products in bulk and then source them to low price markets due to the introduction of parallel trade introduced EU and the UK, and then ship them to high price markets, keeping the high profit difference. The idea of controlling the pricing and reimbursement is becoming a concern as it tightens the value for money and also the growth on managed care is diminishing sales thoroughly. Bargaining Power of SuppliersThe costs of the ingredients needed to manufacture the drug are very low. The major pharmaceutical companies that use in licensing deals and rely on out sourcing the new products manufactured, enable the companies that supply to place a high price on the drugs it will sell although this problem may be offset by the costly R&D processes involved. In future, things such as clinical trials that are costly, outsourcing R&D processes will eventually end in a shakeout leaving major suppliers who can handle the pressure. Threat of new EntrantsThere are high barriers of entry in this industry because of expensive R&D processes, extensive surveillance programs, and long lead times for new drugs to penetrate the market increasing from 3-5% in the 1960s to 12 years in the 1990s. Companies that had a large sales force were among the firms that made the top sales. R&D processes were very costly but also risky because 80 per cent fail to recover the investments made in

the R&D process. Competitive RivalryCompanies that had a large sales force usually used this as a leverage to increase their sales, although being ineffective later as the sales force hardly got any time with the doctors. The great cost of R&D set as a strong exit barrier. Many firms turned to mergers so that they could share the R&D costs, and eliminate any duplicate costs incurred. There was a greater commercial reach through these mergers. It was also a survival strategy for medium sized firms who otherwise would have been dissolved. SWOT AnalysisStrengths: Companies that have high R&D expenditures have the capability of becoming industry leaders because of the competitive edge it provides them and promising growth aspects. Having a large sales workforce also gave the company a very efficient channel to customer base shooting up sales. Firms that have blockbusters usually brought a lot of fortune since these were known as the holy grails of the firms which achieved deep market penetration. Weaknesses: Engaging in R&D is very expensive and risky at the same time. Many firms who have invested in it have lost a lot due to the failure of promising outcomes, many of the latter happening in the late stages of production e. g. BMS and Pfizer. Even though so much is being spent on this process, there is not much show for it because product launches remained below 30 in 2005. Clinical trials which are becoming more costly shoot up expenditure levels. The demand for healthcare is rising but many of the firms are not able to meet this. Opportunities: Alliances coming up are a solution to most of the problems since they allow the development of new inventions and leveraging on economies of scale benefits satisfying the needs and allowing it to compete on a multiple dimensions. Expansion into the EU zone allowed for many

growth opportunities due to unmet needs and a high population indicating prospective long term benefits. Threats: Competition is so aggressive the market. USA and Europe that had gained market growth is now being threatened by countries such as China who have declared that they want to become industry leaders and are already taking action. The use of internet may be an advantage when it comes to reaching out a huge customer base, but it also allows the trade of counterfeit drugs, a black market, which accounts to 10% of the global market. Industry AnalysisDevelopment: The Industry was firmly established in the 1950s. It boomed due to the light regulatory controls and permanent patent protection. Growth: New players appeared in the market, generics being a major competitor. When the thalomide tragedy took place, tighter regulatory controls came into place and legislation set patent expiry to 20 years which opened doors to generics taking over. Governments controlled health care expenditures via pharmaceuticals since they were the easiest target. Biopharmaceuticals were later introduced who were less exposed to generic competition. EU parallel trade was introduced, having a high penetration in the UK, with€4. 2bn recorded revenues but also had a consumer backlash due to the disparity in prices. Emerging markets accounted for 50% of GDP growth in the EU due to high levels of unmet needs and significant long term potential. Shakeout: Collapses of the generic prices in USA lead to determination of cost leadership. The attack of generic drugs on branded had severe effects having sales falling from 18% to 8 %. There was a 40% growth for generics and a 4% decline for patented drugs. Generics was being used as a first line treatment, patented were only used if generic failed. Generics surpassed the

entire market because many blockbuster brands were up for expiry. To counteract these problems, firms increased their sales workforce, tripling revenues. Bio techs were generating high revenues ($63bn) and OTC was also picking up. Maturity: since R&D costs were increasing, many firms were coming up with alliances to survive in the industry. Blockbuster drugs were trying to switch to OTC drugs since they were flourishing better in the industry. Many companies got into disease management initiatives. Decline: 20 blockbusters were about to lose patent protection. Allegra, treatment for hay fever lost 84% sales in just 12 weeks following patent expiry. Clinical trials were becoming more expensive. R&D expenditures were rising, from $231m in 1987 to $1. 48 billion in 2003, leading to mergers to survive in the industry. The demand for healthcare is less than supply creating an unsustainable situation. Many are now rushing to invest in biopharmaceuticals and cancer R&D.