

DTC Public Policy Myths

Does DTC Drive Up the Costs of Consumer-Advertised Products?

The public policy debates on healthcare reform include some contentions that seem to be based more on assumptions than facts. The main assumption seems to be that prescription drug prices are driven higher when a drug is promoted by DTC advertising campaigns.

BY KEN SOBEL

What are the current “talking points” about DTC and pharmaceutical drug pricing? One recurring theme in healthcare public policy debates is that DTC advertising isn’t effective. Another is that the expense of DTC advertising leads to increases in drug prices. Both themes are addressed in a recent study published by the journal *Internal Medicine*¹ and have been widely publicized. The main theme of the reporting on this study is that prices of advertised pharmaceuticals are higher *because* of their advertising expenses.

DTC costs in perspective

To start with, it’s instructive to see just how significant DTC costs are relative to total product revenue. As we see in Table 1, for the 10 brands that had the largest DTC budgets in 2007, the average DTC budget was about \$165 million. Those same brands had average revenues of about \$2.3 billion. This means that DTC costs, on average, represented about 7 percent of product revenues – *and this level is for the brands that emphasize DTC advertising the most*. For the “typical” pharmaceutical product that uses DTC advertising, the percentage is much smaller. The takeaway from these data is that the impact of DTC on product price is at most quite modest.

A different point is also relevant here. Nearly all pharmaceutical companies decide to employ DTC advertising as a tactic only if it returns revenue in excess of its cost. Based on the several hundred DTC evaluation studies I have conducted over the last dozen years, typical values for DTC return-on-investment (ROI) fall in the range of \$1.60 to \$1.90 of incremental revenue per \$1 spent on advertising. If the incremental

Table 1. DTC Budgets and U.S. Sales for the 10 Largest DTC Expenditures, 2007²

	Revenue (\$MMs) ²	DTC Spend (\$MMs) ³	Percent
Lipitor	7,837	157	2
Advair	4,287	136	3
Plavix	3,651	172	5
Vytorin	2,297	136	6
Cymbalta	1,844	144	8
Nasonex	1,030	140	14
Ambien CR	905	175	19
Lunesta	748	307	41
Requip	474	125	26
Rozerem	125	161	129
TOTAL	23,199	1,653	
AVERAGE	2,320	165	7

revenue is expected (or measured) to be less than the cost of the campaign, DTC advertising is typically not employed.

Once this is considered, it's clear that in the absence of DTC advertising, the finances of pharmaceutical brands that currently use DTC advertising would decline. Such a decline might result in an incentive to increase prices, not *because* of DTC advertising but because of its *absence*.

Setting product prices

How are the prices of pharmaceutical products set? The healthcare discussion point that the cost of DTC advertising leads to higher drug prices depends on the implicit assumption that if promotional support budgets go up, pharmaceutical companies respond by increasing the price of the product to help pay for the increased expenses. But this “cost plus” approach to setting prices is at odds with the complicated process that pharmaceutical companies typically go through when they decide on the prices for their products.

Currently, prescription drug prices are set after a complicated set of negotiations, discussion, research, and judgments focused on how attractive and acceptable payers will find the product, and their decisions about the tier level coverage and levels of reimbursement they would provide for the product. If a pharmaceutical product has broad public health benefits (for example, reduces the need for days of hospitalization, lowers absenteeism in the workplace, extends life, etc.), it generally can command strong market access – higher levels of reimbursement and good tier level placement – even at a higher price. Conversely, managers of “me-too” products with fewer outstanding health outcomes benefits will generally need to offer those products at lower prices if they are to avoid substantial market access restrictions.

This means that DTC costs, on average, represented only about 7 percent of product revenues – and this level is for the brands that emphasize DTC advertising the most.

Pharmaceutical companies know that no matter how expensive their promotional plans may be, if they increase the prices of their drugs to a point not justified by the health outcomes that result from patients using their products, they will face market access restrictions that will suppress sales. In other words, prices for prescription drugs are driven by the added value those products can bring to the payer community and not on adding up the costs of promotions and development.

What past experiences reveal

We maintain a database that captures salient facts from the hundreds of DTC forecasting and evaluation projects we have undertaken since the mid-1990s. In nearly half of those cases, one of the issues under study was whether or not DTC should be undertaken at all. For those cases, I compared pricing with and without an anticipated DTC campaign. I found that there are *no differences* in anticipated product pricing when we compare plans with and without the inclusion of a DTC advertising effort.

DTC campaigns do indeed translate into added promotional expenses, but to only a small degree. Of course, they also lead to added revenues, which more than counterbalance the increase in expenses.

Typical values for DTC advertising ROI fall in the range of \$1.60 to \$1.90 of incremental revenue per \$1 spent on advertising.

The further assumption that the increased expenses in turn lead to higher drug prices doesn't hold water. In the first place, the incremental revenue generated by DTC advertising campaigns precludes the “need” for price increases. Secondly, DTC budgets are a very small percentage of overall product revenues, so even without consideration of incremental revenue, the potential impact of DTC on price would be very modest. Finally, and most importantly, the key issues in play when drug pricing is determined are all about health outcomes (for example, facts and judgments about what the market will bear) and don't focus on promotional costs at all, a conclusion confirmed when we examine hundreds of plans laying out anticipated prices for launches with and without DTC advertising support. **DTC**

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References

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- 2 Source: Wolters Kluwer Source® Pharmaceutical Audit Suite (PHAST).
- 3 Integrated WAC dollars.
- 4 Source: “DTC Report – Steady Migration,” MM&M, April 2008, pp. 42-47.