The relevance of a discussion of risk and rate of return to a discussion of pricing in the drug industry may not be immediately apparent, but I think it soon becomes so if we note that any reduction, voluntary or enforced, in the prices charged by the drug industry without simultaneously reducing its costs will flow through to profits immediately. If prices are reduced across the board by administrative fiat, profits will also be reduced.

Now, I do not appear here as an expert on the drug industry, either with regard to its pricing policy or the riskiness of its investments. It requires no such expertise, however, to establish the elementary proposition that for an industry selling an item necessary to life and facing an essentially inelastic demand, changes in price lead immediately to changes in profit in the same direction. It is the drug industry's role as a supplier of necessities that apparently occasions this committee's interest in its pricing policy and it is that same role that establishes the close relation between prices and profits.

Senator NELSON. May I raise just a point here?

You stated that it requires no expertise to establish the elementary proposition that for an industry selling a product necessary to life and facing an essentially inelastic demand, changes in price lead immediately to changes in profit in the same direction. I wonder if that can really stand as an unqualified statement? For example, if a drug is discovered which does something that no other drug does, almost immediately—that is, after some advertising, some understanding on the part of the medical profession—that drug then, if it is a valuable drug, will be in demand in every single case where a patient needs that type of drug. In fact, drugs are more in demand than other products, because health as a general proposition is a prime factor motivating people in pain.

So the demand may be inelastic to the extent that every single person who needs a drug is willing to pay for it. It is not true to automobiles or houses or clothes. So I don't quite follow the statement that the demand is inelastic.

Dr. COOTNER. Well, as a matter of fact, the description you gave is exactly what I would consider inelastic, that is, that the demand is there regardless of price, and I think we are in perfect agreement on the facts.

Senator NELSON. I thought you were using the argument to prove that this was some kind of a handicap to the industry. Whereas, as matter of fact, if there is any other industry that faced this kind of inelastic demand it would be considered a great asset to the industry, wouldn't he, his product?

Dr. COOTNER. Well, that depends, if he had an inelastic demand and he had monopoly power he would certainly like that sort of situation, but inelastic demand in and of itself is no advantage. For example, many people believe, and I think it is probably true, that the American farmer faces essentially an inelastic demand for the same reason, he does not consider that an advantage because it means, as a matter of fact, if the supply increases he is forced to take a substantial cut in price.

Senator NELSON. Not if he had a patent on potatoes. We will get into that some later, but I misunderstood what you were saying about it.