

And then, of course, we may be able to get the product at the retail level at a lower price than for the branded product.

But on your specific point as to whether the branded product sells at the same price or a higher price through drug stores in these comparative bids, I agree with your interpretation of the facts.

Mr. GORDON. I think there may be another point, and that is that the purchasing agent for the ordinary consumer is not the one who pays. In other words, the doctor does not pay for the medicine. He does the purchasing. He orders the drug, and the patient, the consumer, does not have much of a choice.

Dr. MUELLER. I have heard many people speak to that point, including doctors, who say that some doctors are more discriminating in this respect than others. And I think increasingly, with publicity concerning the alternatives available, consumers often ask their doctors: "What is this generic business all about?" So this, I suspect, makes the doctor a little bit more price conscious. And I think this is one of the benefits of publicity concerning the alternatives available to consumers. It is sort of a counter to the advertising which promotes brand names so decisively in the minds of consumers today.

Senator NELSON. Go ahead.

Dr. MUELLER. The resulting wide price spread between advertised and generic drugs often applies to unpatented as well as patented drugs. These factors shelter the leading concerns, or any concern with a highly differentiated drug product, from effective price competition.

This explanation of high drug profits is not novel. Nearly all researchers who have analyzed the drug industry in detail have come essentially to the same conclusion. Similarly, empirical studies which have cut across many industries have identified the elements of market structure that are primarily responsible for high noncompetitive profits. These elements are high seller concentration, high barriers to entry, and product differentiation.

Mr. GORDON. Dr. Mueller, for the record, will you please explain exactly what product differentiation is?

Dr. MUELLER. I had anticipated this question. I know that Senator Nelson was an undergraduate student in economics but now is primarily a lawyer—or, I should say, primarily a statesman.

Senator NELSON. You may make that statement here, but no place else.

Dr. MUELLER. I am thinking of back in Wisconsin.

There is a definition of product differentiation which appears in the Antitrust Law and Economic Review which, presumably, is written for lawyers. I am not sure if this is an improvement on one that I could make for students.

That is the way they define it—they say:

Product differentiation refers to the distinguishing of substitute products from one another by advertising and the like. Whereas buyers of homogenous products regard the output of any particular seller as identical in all respects to that of all other producers of that product, the seller of a "differentiated" product enjoys a favored position over its rivals, in that the buyers consider it a superior product and are willing to pay a "premium" price for it rather than accept the substitutes offered by those rivals. Since new entrants must frequently accept a lower price than established firms are able to get for a product of equal quality and cost, this disadvantage is said to constitute a "barrier to entry," one that permits established firms to charge a supercompetitive price without attracting new entry.