high profit industry where established firms hold a strong position relative to small companies and potential entrants. The industry is frequently described as "depression resistant" because, as one analyst put it, "Illness is no respector of business cycles, and Americans have shown that they will buy the medicine they need regardless of economic conditions." These characteristics are considered to make drug stocks good "defensive" investments. As a result, drug stocks sell at relatively high price-earnings ratios, indicating that investors are confident of a high future payout. A Standard & Poor's analysis of drugs summed up the factors affecting drug stocks as an investment as follows:

> Shares of drug equities have historically sold at relatively high price-earnings ratios, owing to the industry's recession-resistant characteristics, its above-average earnings growth rate, and its strong underlying position. Moreover, it is difficult to enter the drug field.

Investment analysts generally emphasize that the high earnings of drug companies make drug stocks a good buy. This is not to imply, of course, that investment analysts view the industry as completely riskless. The staff of Moody's Investors Service, after explaining a number of reasons why drug stocks were a good investment, stated:

> The drug industry cannot be risk-free. The postwar years have seen periods of slowdown, and individual companies have suffered temporary setbacks. The causes have been many. Competition has led to price-cutting in popular products, such as penicillin, where capacity has been overexpanded. Occasionally, a profitable new drug is found to have unsuspected and unfavorable side effects. This, however, is less of a problem than product obsolescence or the expiration of patents on major drugs that have been exclusive with one company. In recent years, government regulation has been tightened at the drugmaker's expense. Finally, the ebb and flow of respiratory diseases often causes sharp fluctuations in drug sales.

But after enumerating the above points, the Moody's analysts continued:

> The impact of such development has caused only temporary deviations in a growth curve that has pointed strongly upward.

Thus, while the drug industry faces uncertainties and problems, from an investor's standpoint these "risks" apparently are no greater than those found in many other industries. On the contrary, drugs are considered a sound growth investment.

Investment analysts frequently make mention of the fact that drug profits may be adversely affected by factors that will increase price competition and thereby erode high profits. The most frequent reference of this sort is the observation that anything threatening to increase the use of generic drugs as opposed to brand name drugs threatens high profits. An analysis by "Value Line" of the possible effects of medicare on drug profits is typical of investment analysts' views on the subject. After explaining that medicare very probably would increase drug sales, "Value Line" concluded that drug profits would not go up by a corresponding amount because:

> Hospitals and institutions usually, wherever possible, buy generic name drugs rather than brand names in order to reduce costs. *The most profitable business for the drug manufacturers is that which comes through drugstores, where drugs are prescribed on a brand name basis.* [Emphasis added.]