TABLE 2.—RATES OF RETURN OF DRUG MANUFACTURERS AND ALL MANUFACTURING INDUSTRIES, 1956–67

Year	Profits after taxes as a percent of stockholders' equity		Profit rank of the drug industry among all manufacturing industries [1]
	All drug manufacturers	All manufacturers	
1956	17.6	12.3	2
1957	18.6	11.0	1
1958	17.7	8.6	1
1959	17.8	10.4	1
1960	16.8	9.2	1
1961	16.7	8.8	1
1962	16.8	9.8	1
1963	16.8	10.3	1
1964	18.2	11.6	1
1965	20.3	13.0	1
1966	20.3	13.5	2
1967 (3 quarters)	18.6	11.5	1

[1] Rank among the 26 industries for which profits are reported separately in Quarterly Financial Reports.
Source: Federal Trade Commission and Securities and Exchange Commission, Quarterly Financial Report.

Since the first such article appeared in 1962, there has been a growing volume of research literature on the subject, all of which has drawn heavily on the Kefauver and subsequent Congressional hearings. The facts developed by this committee have made another enormous contribution to the fund of knowledge concerning the drug industry. I am confident that scholars will be sifting and winnowing the facts for years.

THE CAUSES OF HIGH PROFITS IN THE DRUG INDUSTRY

The preponderance of economic evidence argues that the persistently high profits of the drug industry are the result of the absence of effective price competition in the sale of many products. Price competition in drugs in ineffective for several reasons. Concentration in the production of many drugs is high because of the patent privilege.[4] And even where there are relatively many sellers, as well as many potential sellers (for example, in the case of unpatented drugs sold under generic names), effective price competition often is muted by vast advertising, promotion, and other selling effort which differentiates in the minds of consumers the products of the largest drug manufacturers selling under their own brand or trade names from those of other manufacturers.[5] Hence, manufacturers selling chemically identical drugs under generic names frequently have difficulty in selling them at any price. The resulting wide price spread between advertised and generic drugs often applies to unpatented as well as patented

[4] The Kefauver committee staff analyzed concentration for 51 products in the major drug groupings: antibiotics, hormones, diabetic drugs, sulfas, vitamins, and tranquilizers. These products represented at least two-thirds of the total value of ethical drugs in 1958. The 15 leading drug companies controlled the production of these important products as follows:

"In 27 of the products, or more than one-half the entire U.S. output is produced by 1 of the 15 companies. . . . In sulfa drugs, one company accounts for 100 percent of the output in eight of the nine products. In tranquilizers the condition of monopoly prevails in six of the seven products. In antibiotics (other than penicillin) the total output is produced by one company in five of the nine products, and in hormones and vitamis, each, in three out of the nine. In 8 additional products concentration takes the form of "duopoly"—control by 2, while in 10 others the entire output is produced by 3 companies. Against the typical structure of concentration in manufacturing industries, it is indeed remarkable that in only 6 of the 51 products are there as many as 4 producers."

Report No. 448 of the Committee on the Judiciary, U.S. Senate, made by its Subcommittee on Antitrust and Monopoly, 87th Cong., First Sess., *Study of Administered Prices in the Drug Industry,* June 27, 1961, pp. 68–69.

[5] It well recognized that advertising and promotion effort in the drug industry is greater than it is in nearly all other large American industries. See, for example, William S. Comanor and Thomas A. Wilson, "Advertising, Market Structure, and Performance: An Empirical Analysis," *Review of Economics and Statistics,* November 1967, Appendix Table 2. Of the 41 industries studied by Comanor and Wilson, all but two had lower advertising-to-sales ratios than did drug manufacturers. Comanor and Wilson further point out that advertising outlays represent less than half of the total selling expenditures of drug companies.