Pharmaceutical Innovation and Parallel Trade

BACKGROUND

- Parallel imports are genuine goods produced under the protection of a patent, a trademark or copyright and then imported into a second market without the authorization of the owner of the intellectual property right.
- Parallel trade exists when there are significant price differences between countries making this trade attractive.
- International price differences can be sustained only if intellectual property rights are fully protected, making the creator the exclusive owner of her innovation: the patent holder may be expected to exert market power by charging a different price in different markets for the same or similar goods.
- This form of third-degree price discrimination yields ambiguous welfare effects.

METHODOLOGY

- The authors focus on the pharmaceutical sector in examining how different regimes of intellectual property rights interact with specific features of government intervention, namely price cap regulation.
- The analysis is based on the strategic interaction between a single innovative firm located in the unregulated North, and a foreign government located in the South.
- A complete welfare analysis is provided that accounts for both global investment decisions in R&D as well as the local costly distribution of drugs.
- The patent holder's decisions are examined when a foreign government can introduce a direct price control to lower the price of patented drugs.

KEY FINDINGS

- The authors clarify the circumstances under which parallel trade, despite weakening intellectual property rights, can actually create higher incentives to conduct R&D. This higher investment also translates into higher global welfare.
- It is shown that, under parallel trade, investment can rise only when the foreign government takes into full account its impact both on investment and on the firm's decision to supply the regulated country. This occurs because of a complete withdrawal from price regulation.
- However, the regulated country is better off under an intermediate form of commitment whereby the foreign government anticipates its effect only on local distribution and delivery but not on global R&D investment. In this case, the government resorts to some price regulation which reduces investment, in particular, under parallel trade.

POLICY ISSUES

- Parallel trade makes government policies interdependent and forces every government to consider the consequences of its actions on global incentives to invest. Therefore, a balanced approach towards evaluation of the costs and benefits of allowing parallel imports should fully incorporate the strategic effects of the regulatory regime on the level of both the price and quality of drugs.

W: www.competitionpolicy.ac.uk
T: +44 (0)1603 593715
A: UEA, Norwich, NR4 7TJ

University of East Anglia

E·S·R·C ECONOMIC & SOCIAL RESEARCH COUNCIL

An ESRC Research Centre
CCP CENTRE FOR COMPETITION POLICY

June 2012

Pharmaceutical Innovation and Parallel Trade

CCP Policy Briefing

An ESRC Research Centre

CCP
CENTRE FOR COMPETITION POLICY

June 2012

Pharmaceutical Innovation and Parallel Trade

CCP Policy Briefing

THE CCP

The ESRC Centre for Competition Policy (CCP), at the University of East Anglia, undertakes competition policy research, incorporating economic, legal, management and political science perspectives, that has real-world policy relevance without compromising academic rigour.

FOR MORE INFORMATION

The full working paper (12-9) and more information about CCP and its research is available from our website: www.competitionpolicy.ac.uk

ABOUT THE AUTHORS

- Anna Rita Bennato is a Post Doctoral Researcher at the CCP.
- Tommaso Valletti is a Professor at Imperial College London.

W: www.competitionpolicy.ac.uk
T: +44 (0)1603 593715
A: UEA, Norwich, NR4 7TJ

UEA University of East Anglia

E·S·R·C ECONOMIC & SOCIAL RESEARCH COUNCIL