

MOH Rethinks Costs

Pharmaceuticals

Japan produced ¥5.7503 trillion worth of pharmaceuticals in 1995. This figure represents a 1% increase over the previous year, and is the second increase in as many years. But it is the lowest increase since 1989, when production grew by 8.9%.

The Ministry of Health and Welfare (MOH) exerts tremendous influence over the Japanese pharmaceutical industry because sales in this industry are about 95% dependent on the domestic market. Pharmaceutical prices are set by the government, and have been steadily cut since 1981. Financial concern about the rising cost of health care has prompted the government to try to keep a lid on medical costs. Japan's pharmaceutical prices are higher than those in Europe or the U.S. in spite of the trend in price reductions. Because national health insurance covers the actual cost of whatever medicine is used (rather than fees paid for services rendered), the tendency is to use higher priced brands and larger quantities of medicine, thereby raising the overall cost of medical care.

Such policies protect the pharmaceutical industry, which has enjoyed exceptionally high profits compared to other domestic industries. But in recent years, the MOH has begun to change its stance and has taken steps towards lightening its financial burdens. The ministry has broadened the application of fixed and lump sum payments in place of the current system to include many aspects of in-hospital care for the elderly. It also gives incentives to both patients and doctors to keep down their medical costs. In 1993, the ministry first proposed the use of generic products, and as fixed and lump sum payments become more widespread, so will demand for cheaper generic medicines for chronically ill patients and others. The MOH is considering dropping some drugs from national health insurance coverage and raising the patient's

cost-sharing responsibilities. Such government actions will have a strong impact on both the quality and quantity of demand for pharmaceuticals.

The age in which the MOH's welfare policies expanded demand for medical drugs and protected domestic industry is coming to an end, and as a result we can no longer anticipate the growth of the pharmaceutical market to much exceed the growth rate of GNP.

Compared to the pharmaceutical development companies of Europe and the U.S., Japan's pharmaceutical corporations are much less profitable. There are two main reasons for this. First, because their weak research and development capabilities have produced few original products for the international market, they have to rely on domestic versions of foreign-developed products, which are less profitable. Second, because there is little to distinguish the products of various companies, competition is intense. This, coupled with large numbers of employees (especially in the sales sector) boosts costs for the entire industry.

To combat this, pharmaceutical companies protect growing profits by lowering operating costs and restructuring management. However, the deteriorating conditions mentioned above are forcing pharmaceutical wholesalers into selective competition through absorption and mergers. There are also two mid- to long-term issues for the industry. First, as developing new pharmaceuticals becomes more and more difficult, research and development requirements may squeeze profits. Second, the International Conference on Harmonization of Technical Requirements for Registration of Pharmaceuticals for Human Use, is promoting the international harmonization of technical standards by developing a multilateral applications process for new pharmaceutical approval. This will lower barriers to entering major markets, but will also make the screening

process in Japan more stringent.

European and U.S. pharmaceutical companies, like their Japanese counterparts, are experiencing an ever harsher business environment, and are fast using mergers and other drastic tactics to strengthen their industries. Japan's industry must likewise shore up its competitiveness by investing more in research and development.

Biochemistry

According to a survey by Nikkei Biotech, Japan's biomedical market shrank for the first time in 1994, by 0.7%, to ¥606.6 billion. The main reason for this end to the industry's fast growth was the sudden drop in the market for Interferon, a medicine used to treat Hepatitis C, a rapidly emerging disease. In 1993, the market for Interferon was ¥200 billion. But in April 1994, pharmaceutical price revisions slashed the price of the drug. In addition, most patients had been administered Interferon once, and second-time use was not approved. The market thus shrunk to ¥60 billion, and is predicted to drop to ¥55 billion in 1995. At this level, even growth in other sectors of the industry could not reverse the stagnation of the industry as a whole.

The groundwork for commercial applications of biotechnology is nevertheless progressing steadily. Guidelines for genetic engineering of agricultural products have been published. Operations will start at the earliest in spring 1996, opening the way for direct use of recombinant agents. Guidelines for safety and quality control of genetic therapy pharmaceuticals have been also approved, marking the beginning of commercial use of genetic therapy.

However, the biotech market is unlikely to take off in the near future, as further research and development is needed to prepare for the 21st century.

(Yokoo Hisaaki, senior economist)