

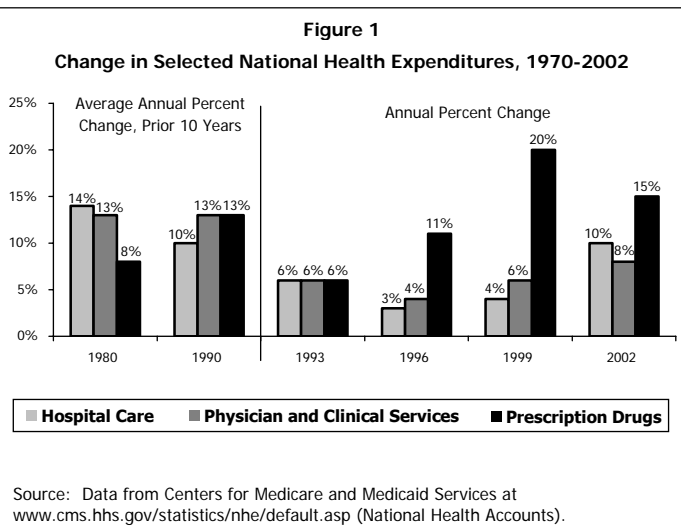
## PRESCRIPTION DRUG TRENDS

### Overview

National attention is focused on prescription drugs because of rapidly rising prescription costs and issues relating to implementation of the new Medicare drug benefit. Growing concerns about the affordability of needed drugs, coupled with the significant profitability of drug manufacturers, are causing policymakers and others to consider new approaches to addressing drug costs.

### Rising Expenditures for Prescription Drugs

Spending in the U.S. for prescription drugs was \$162.4 billion in 2002, 4 times larger than the amount spent in 1990. Although prescription drug spending is a relatively small proportion (11%) of national health care spending, it is one of the fastest growing components, increasing at double-digit rates in each of the past 8 years. National prescription spending increased 15% from 2001 to 2002, compared to an 8% increase for physician and clinical services and a 10% increase for hospital care (Figure 1).

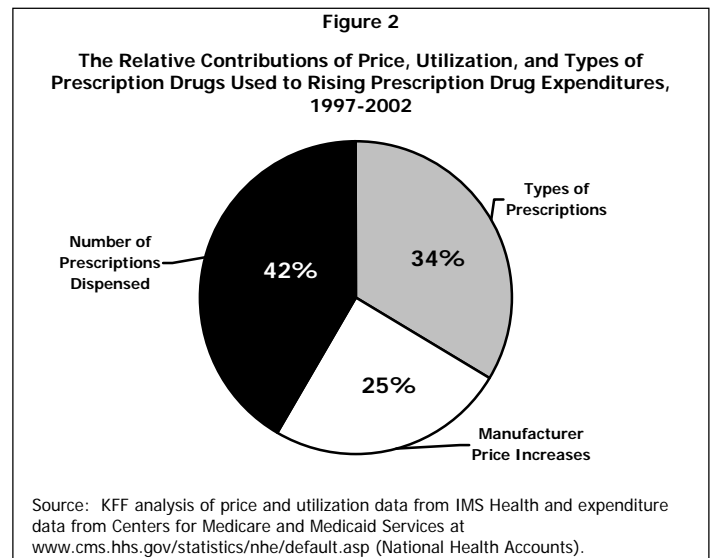


### Factors Driving Increases in Prescription Spending

Three main factors are driving the increases in prescription drug spending (Figure 2):

- *the increasing number of prescriptions* (utilization) was responsible for 42% of the overall increase in prescription spending from 1997-2002;

- *changes in the types of drugs used* (with newer, higher-priced drugs replacing older, less-expensive drugs) accounted for 34% of the increase; and
- *manufacturer price increases for existing drugs* accounted for 25% of the increase.



Among the key trends are:

- **Utilization.** From 1993 to 2003, the number of prescriptions purchased increased 70% (from 2.0 billion to 3.4 billion), compared to a U.S. population growth of 13%; the average number of prescriptions per capita increased from 7.8 to 11.8.<sup>1</sup>
- **Price.** Retail prescription prices (which reflect both manufacturer price changes for existing drugs and changes in use to newer, higher-priced drugs) have increased an average of 7.4% a year from 1993-2003,<sup>2</sup> more than double the average inflation rate of 2.5%.<sup>3</sup>
- **Changes in Types of Drugs Used.** Most of the top-selling prescriptions are newer, higher-priced brand name drugs, whose availability is affected by the research and development (R&D) activities of pharmaceutical manufacturers and government-supported research. Manufacturer R&D spending increased from \$12.7 billion in 1993 to an estimated \$33.2 billion for 2003, with R&D estimated to be 17.7% of sales in 2003.<sup>4</sup> New drug use is also affected by the number of new drugs (new molecular entities) approved by the U.S. Food and Drug Administration, typically about 30 a year over the past 10 years, but only 21 in 2003.<sup>5</sup>

From 1995-2002, pharmaceutical manufacturers were the nation's most profitable industry. In 2003, they ranked third, with profits (return on revenues) of 14% compared to 5% for all Fortune 500 firms.<sup>6</sup>

Both prescription use and shifts to higher-priced drugs are affected by advertising. Manufacturers spent \$25.3 billion for advertising in 2003, with \$22.1 billion (87%) directed toward physicians (including \$16.4 billion for the retail value of drug samples), and \$3.2 (13%) billion directed toward consumers. Spending for direct-to-consumer advertising -- typically to advertise newer, higher-priced drugs -- was over 8 times greater in 2003 than in 1995.<sup>7</sup>

### Insurance Coverage for Prescription Drugs

In 1996, 23% of nonelderly Americans had no drug coverage (more recent data are not available), including those without any health insurance for some or all of the year.<sup>8</sup> Additionally, more than a third (36%) of Medicare beneficiaries had no prescription drug coverage in the Fall of 2001.<sup>9</sup> Under the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, Medicare will offer a voluntary prescription drug benefit beginning in 2006.

Lack of drug insurance can have adverse effects. A recent survey found that 37% of the uninsured said they did not fill a prescription because of cost, compared to 13% of the insured.<sup>10</sup> A 2001 survey of seniors in 8 states (42% of US adults age 65+) found that in the last 12 months, 35% of seniors without prescription drug coverage either did not fill a prescription 1 or more times or skipped doses of medicines to make the prescription last longer, compared to 18% with drug coverage.<sup>11</sup>

### Private and Public Responses

Employer-sponsored health plans have responded to increasing prescription drug costs by establishing tiered cost-sharing formulas and increasing drug copayments. In 2004, a majority (68%) of workers with employer-sponsored coverage have at least 3 tiers of cost-sharing arrangements, two and a half times the proportion in 2000 (27%). Copayments for nonpreferred drugs (those not included on a formulary or preferred drug list) have increased 94% during the same time period, from an average of \$17 per prescription in 2000 to \$33 in 2004. Copayments for preferred drugs (those included on a formulary or preferred drug list, such as a brand name drug with a generic substitute) increased by 62%, from \$13 in 2000 to \$21 in 2004.<sup>12</sup>

Cost containment initiatives in the area of prescription drugs were implemented by 47 states and the District of Columbia in FY2004 for Medicaid, the public program that plays a key role in providing outpatient pharmacy services to the low-income population. These initiatives included making more drugs subject to prior authorization (33 states) and having preferred drug lists (27 states). For FY2005, 43 states have indicated they would implement new or additional pharmacy-related initiatives, including preferred drug lists (29 states),

seeking supplemental rebates (26 states), and making more drugs subject to prior authorization (21 states).<sup>13</sup>

### Outlook for the Future

U.S. spending for prescription drugs is projected to increase by 10.7 percent annually between 2004 and 2013.<sup>14</sup> This is a slower growth rate than we have seen in recent years, with the slowdown due in part to fewer new drugs being introduced into the market, a reduction in direct-to-consumer advertising, the impending loss of patent protection for some leading drugs, new cost-sharing provisions in private insurance contracts, and a lower rate of price growth.<sup>15</sup> On the other hand, implementation of the new drug benefit in Medicare is likely to increase aggregate drug spending by improving the financial access of elderly and disabled Medicare beneficiaries to prescription drugs.

<sup>1</sup> IMS Health website at [www.imshealth.com](http://www.imshealth.com) and Census Bureau at [www.census.gov](http://www.census.gov). The 2003 number of prescriptions per capita (11.8) differs from the 10.8 on [www.statehealthfacts.kff.org](http://www.statehealthfacts.kff.org) because the data come from different sources (IMS Health vs. Verispan).

<sup>2</sup> National Association of Chain Drug Stores, "Industry Facts-at-a-Glance," at [www.nacds.org](http://www.nacds.org), using data from IMS Health.

<sup>3</sup> Bureau of Labor Statistics at [www.bls.gov](http://www.bls.gov).

<sup>4</sup> Pharmaceutical Research and Manufacturers of America, *Pharmaceutical Industry Profile*, various years, at [www.pfma.org/publications](http://www.pfma.org/publications).

<sup>5</sup> US Food and Drug Administration at [www.fda.gov/cder](http://www.fda.gov/cder).

<sup>6</sup> *Fortune*, April 5, 2004.

<sup>7</sup> IMS Health website at [www.imshealth.com](http://www.imshealth.com). Physician promotion excludes amounts for professional meetings and events.

<sup>8</sup> US Department of Health and Human Services, *Prescription Drug Coverage, Spending, Utilization, and Prices: Report to the President*, April 2000.

<sup>9</sup> Kaiser Family Foundation, *Trends in Medicare Supplemental Insurance and Prescription Drug Benefits, 1996-2001*, M. Laschober, June 2004.

<sup>10</sup> Kaiser 2003 Health Insurance Survey, 2003.

<sup>11</sup> Kaiser Family Foundation/The Commonwealth Fund/Tufts-New England Medical Center, *Seniors and Prescription Drugs: Findings From a 2001 Survey of Seniors in Eight States*, July 2002, p.25.

<sup>12</sup> Kaiser Family Foundation and Health Research and Educational Trust, *Employer Health Benefits: 2004 Annual Survey*, September 2004.

<sup>13</sup> Kaiser Commission on Medicaid and the Uninsured, *The Continuing Medicaid Budget Challenge: State Medicaid Spending Growth and Cost Containment in Fiscal Years 2004 and 2005: Results from a 50-State Survey*, October 2004.

<sup>14</sup> *Health Affairs*, "Health Spending Projections Through 2013," Feb. 11, 2004, at [www.healthaffairs.org](http://www.healthaffairs.org). Note that this projection does not take into account the impact of the Medicare Modernization Act of 2003.

<sup>15</sup> *Health Affairs*, "Health Spending Projections Through 2013," Feb. 11, 2004, at [www.healthaffairs.org](http://www.healthaffairs.org).

### For More Information

This Fact Sheet (#3057-03) and the following reports are available on the Kaiser Foundation's website at [www.kff.org](http://www.kff.org): *Trends and Indicators in the Changing Health Care Marketplace, 2004 Update* (#7031), *Prescription Drug Trends—A Chartbook Update* (#3112), *Medicare and Prescription Drugs* (#1583-06), *Medicaid Prescription Drug Spending and Use* (#7111), *Medicaid and Prescription Drugs* (#1609-02), *Federal Policies Affecting the Cost and Availability of New Pharmaceuticals* (#3254), *Employer Health Benefits, 2004* (#7148), *Retiree Health Benefits Now and in the Future*, (#6105). See also [www.statehealthfacts.kff.org](http://www.statehealthfacts.kff.org) for state-specific prescription drug utilization, sales, and average prices (under Health Costs & Budgets).