DUFF & PHELPS

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# Understanding Cost of Goods and Pricing for Product Development Partnerships

PDP Access Group

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# Key questions for Discussion

- **Why is industry so reluctant to share COGS data?**
- **How does industry think about the link between COGS and price?**
- **What are major COGS categories and drivers?**
- **What are typical expectations for return on investment for industry?**
- **How does industry think about "access agreements" and "access pricing"?**
- **What happens to COGS when production volume increases significantly?**

# Sharing COGS Data

- **Manufacturers are reluctant to share COGS data because the data expose margins and may change expectations on pricing.**
- **For biopharma companies in particular, prices to different customers vary widely, and margins can appear to be very high.**
- **Manufacturers are very concerned about reference pricing, and the potential that, if discovered, COGS data could be used as leverage to reduce prices.**

# Relationship between COGS & Pricing

- **In many cases there is absolutely no relationship between COGS and pricing.**
- **PREVNAR pricing was considered by many to be a fundamental shift in vaccine economics and was established based on health economics.**
- **Price increases are often linked to general inflation measures rather than true increases (or decreases) in production costs over time.**
- **At very low rates of return, the cost accounting methods become very important in determining price.**

# Major Categories of Industry COGS

- **Research & Development**
  - **R&D expense is usually significant, may be treated as a "portfolio" cost, and timing/depreciation assumptions are very important. Includes pre-clinical and clinical trial costs.**

- **Fixed Costs**
  - **Fixed costs are usually driven by plant and equipment. Shared facilities and specialty equipment require careful analysis. Depreciation rates, location, and taxation are important considerations.**

- **Variable Costs**
  - **These range from true variable costs (e.g., vial, stopper, etc.) to more complicated costs that may not increase linearly as volume increases. Allocation is important for high-volume production.**

- **Other Costs**
  - **Include royalties, taxes, transfer pricing, etc.**

# Expected rates of return

**Manufacturers have expectations on rates of return that vary by product / project:**

- **Cost of capital**
- **Risk profile of investment**
- **Franchise value**
- **Available capacity**
- **Volume & other commitments from purchaser**
- **Competition**
- **“Soft” considerations**

# Other Considerations

- Reputation vs. Economic Return
  - Manufacturers may be willing to reduce their expectations for economic return if there is an opportunity to enhance corporate reputation

- Lifecycle Considerations
  - It is probably easier to negotiate better “access” pricing towards the end of the product lifecycle.  However this continues to promote health access disparities.

- Is there a trend towards better prices for low-income markets?

- Price transparency

- Role of PAHO