

Big Pharma's Delicate Dance on Drug Prices

Merck CEO Kenneth Frazier talks about pricing, R&D—and why big pharmaceutical companies aren't admired like they once were



KENNETH FRAZIER | 'A lot of the basic research has become more distributed' at smaller companies. *PHOTO: MICHAEL LUND* By Peter Loftus Feb. 21, 2016 10:05 p.m. ET

Drug makers are enjoying a research-and-development revival after a fallow period. Last year the U.S. Food and Drug Administration approved 45 new drugs, more than double the number in 2006.

But the industry also faces growing criticism of the prices it charges for new drugs—some cancer therapies cost as much as \$150,000 a year—as well as repeated price increases for older drugs. Critics say high prices are putting drugs out of reach for many patients and straining health-care budgets.

Kenneth C. Frazier is in the thick of both the R&D and pricing issues. As chief executive of [Merck MRK -0.45 %](#) & Co. since 2011, he has tried to revive Merck's once formidable R&D engine, which hit an unproductive patch in the late 2000s and early 2010s. A milestone in Merck's turnaround efforts was the 2014 introduction of Keytruda, a drug that stimulates patients' immune systems to fight cancer.

Mr. Frazier, who serves as chairman of the industry lobbying group Pharmaceutical Research and Manufacturers of America, says the industry must do more to address pricing concerns. But he defends premium pricing for some drugs as a necessary incentive for companies to take on risky drug-research projects.

Mr. Frazier, 61 years old, who joined Merck as an in-house attorney in 1992, discussed pricing and R&D challenges in an interview on the sidelines of the J.P. Morgan health-care conference in San Francisco in January. Edited excerpts follow.

The pricing challenge

WSJ: *The increase in prices for branded drugs is getting a lot of attention. Merck has raised prices for drugs like the Type 2 diabetes treatment Januvia. What is your explanation?*

MR. FRAZIER: Merck has increased the prices of its drugs on a yearly basis, but we've tried to be constrained in how we've done it, in a way we think doesn't prevent people from affording our drugs. There's a huge challenge we face between trying to optimize access to our drugs in whatever pricing we establish, and trying to ensure that you have the resources to continue to pursue the next generation of drugs. We try to take a responsible, balanced approach.

WSJ: *So the prices are helping you fund R&D?*

MR. FRAZIER: In part, yes. We have to have a sustainable model. We have to be able to attract sufficient capital. The window in which we can actually make our investment back is a very short window, before drugs go off patent. Having said that, I still think there's a challenge we have in the industry with respect to pricing and annual price increases that we're going to have to think through. We're going to have to find new and better ways to link what we charge for the drug to the value that it actually creates in the marketplace.

WSJ: *What would be a way to link the price of drugs to the value they bring?*

MR. FRAZIER: For example, charging people a price commensurate with the actual outcomes that drugs produce. Now, there are a lot of barriers in the system to sharing risk with some of our customers. The laws around what we can and cannot do in our pricing model were made for a different environment. They weren't made for performance-based

contracting or risk-sharing or any of those kinds of experimental approaches to pricing that Merck actually is very eager to try out with some of its customers.

WSJ: *Is the debate over drug prices having an effect on companies like Merck?*

MR. FRAZIER: I think what it's causing us to do is to engage more in helping the public understand the connection between the cost of today's drugs and the need for the capital to be invested in tomorrow's drugs.

Better research

WSJ: *Merck has a legacy of innovative R&D but has had some rough patches in recent years. Could you explain the changes you've made?*

MR. FRAZIER: Merck has had a legacy of scientific leadership, and that has resulted in many first-in-class medicines that have revolutionized patient care. We can't live in our past, however. Our aim is to be the company that comes forward with medically important products that make a difference in the world. A lot of what I've been trying to do since I have been CEO is to ensure that we have in place the right culture and the right leadership to allow Merck to restore itself as one of the premier, if not the premier, biopharmaceutical research organizations in the world.

WSJ: *It seems like there has been a shift among big pharmaceutical companies to be more externally focused.*

MR. FRAZIER: I think that's right. If you went back 40 years, bright scientists in academia who wanted to come to industry saw the large pharma industry as their port of entry, and they probably would spend their career here. Now, with the freer availability of venture capital and financing, you have people who are starting smaller companies that are going after particular targets of interest to those academics. So a lot of the basic research has become more distributed.

And so for a company like Merck to be successful, we have to be interacting with a whole constellation of smaller players, and we have to be very discerning in our interactions to make sure we have the best external research.

WSJ: *What lessons can a big company like Merck learn from smaller drug developers?*

MR. FRAZIER: One of the challenges associated with a company becoming large is that companies become hierarchical. They become bureaucratic. They become slow. They become risk averse. What [Merck R&D chief Roger Perlmutter] has tried to do since he's come back to the labs [in 2013] is, he's trying to free up scientists from the burden of bureaucracy so that they can focus on doing science. Nobel quality?

WSJ: *Merck used to top the lists of most-admired companies. Why doesn't that happen anymore, and what can be done to try to restore that?*

MR. FRAZIER: There was a run at Merck from late '80s to early '90s of incredible innovation, one after another, which is what led people to admire the company so much. So I hope to restore Merck as an innovation powerhouse.

What is different is the industry is viewed in a different light than it was in the 1990s. It's hard to imagine a pharmaceutical company getting the kinds of accolades we used to get then. We still believe Merck has an important role to play in the world. It's just that the world's a lot more complex than it was back then, and I think the entire pharmaceutical industry has a lot of work to do to restore public trust. If you look at the Nobel Prize being given to a [former] Merck scientist, Bill Campbell [in October, for his work on a treatment for river blindness in tropical regions], I think that's a recognition of Merck's contributions in terms of its scientific excellence.

WSJ: *Do you think Merck is doing the kind of work now to produce another Nobel?*

MR. FRAZIER: Yes, I do. I think the work we are doing is changing the world. Look at Keytruda. It's a big deal. If we're lucky enough to get a positive result in Alzheimer's, that's a huge contribution to mankind. The first vaccine for cervical cancer, those are huge advances. And I could go on.