PRI CENTER FOR MEDICAL ECONOMICS AND INNOVATION

Drug Manufacturers Earn a Lower Return on Capital Than PBMs and Health Insurers

Advocates of drug price controls rely on the misconception that innovative drug manufacturers are earning excessive returns – they are price gouging. Such assertions fail to account for the long, risky, and expensive process required to develop innovative medicines. Accounting for risks and the exceptionally high capital costs, the financial returns of drug manufacturers are below average, which demonstrates that the allegations from drug price control advocates are ill-founded.

Developing medicines is a risky, capital-intensive process

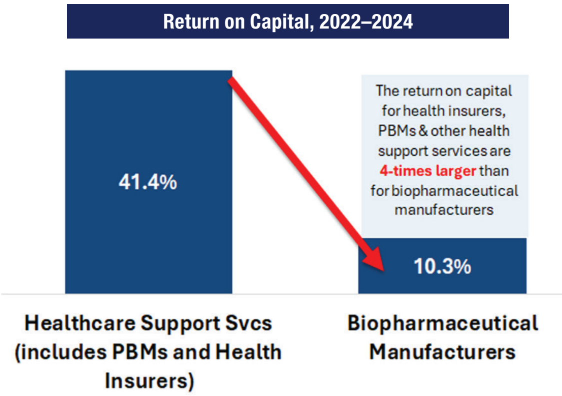
Biopharmaceutical development is among the most capital-intensive and high-risk activities in the U.S. economy. Companies invest billions of dollars over long periods to research, test, and gain approval for new therapies.

Most drug candidates fail somewhere along the way, meaning much of the capital invested never produces any return. The profits earned on successful drugs must cover their own development costs and the costs of the many failed efforts.

Overall, biopharmaceutical companies invest 33.2% of their sales back into R&D activities compared to 3.8% for U.S. companies excluding financials.[1] Healthcare support services, such as pharmacy benefit managers (PBMs) and insurers, invest a mere 0.1% into R&D.

Accounting for the risks and large capital requirements, manufacturers' returns are not excessive

A more accurate and insightful profitability measure for R&D intensive industries is profits relative to the amount of money invested in the business (i.e. capital).



Based on this metric, biopharmaceutical companies generated a 10.3% profit rate between 2022 and 2024.[2] This is the lowest profitability rate relative to all other health care industries and even below the 15.2% average return for all U.S. industries (excluding financials).[3] Health insurers, pharmacy benefit managers (PBM), and other health services companies earned a 41.4% return on capital, **a profitability rate that is 4-times larger than biopharmaceutical manufacturers.**

PBMs and insurers earn higher returns on capital largely because they require much less capital investment and face lower risk. These businesses rely on administrative systems like claims processing and formulary management and benefit from steady demand and vertically integrated models. Because relatively little capital is at risk, even seemingly moderate profits mean high returns and do not reflect greater innovation or productivity.

Accounting for risks and the large capital investments, biopharmaceutical manufacturers earn below average returns.

1 Pham, Pipes and Winegarden "Imbalance of Financial Risks and Economic Rewards in the U.S. Healthcare Supply Chain" Pacific Research Institute, January 2026.

2 See: Pham, Pipes and Winegarden. Return on capital = Operating income after tax / (Book value of equity + Book value of debt – Cash).

3 The biotech sub-industry, accounting for about 45% of the biopharmaceutical industry, had a modest 3.7% return on capital, compared with 15.7% for the pharmaceutical sub-industry. During the same period, the biotech sub-industry allocated nearly 44% of its revenues to R&D, whereas the pharmaceutical sub-industry allocated 22%.