Conclusion for Equilibrium Price Dispersion in Retail Markets for Prescription Drugs, Sorensen (2000)

The purpose of this study is to establish the empirical importance of price dispersion due to costly consumer search by examining retail prices for prescription drugs. The research was conducted in two different locations in order to test the geographical factor whether it had its effect on prices of pharmacies within the same market. The result showed that prices in two geographically distinct mar- kets are shown to vary considerably across pharmacies within the same market. According to the empirical analysis on the observation of consumers to see what is their incentives, it indicated that their incentives are based on characteristics of drug therapy, which price distribution has cross-sectional patterns that are in line for the predictions of this research's model that is prices for repeatedly purchased prescriptions show significant reductions in both dispersion and price-cost margins, as the expected benefits are highest. The research mentioned that the absolute dispersion of prescription prices to decrease with purchase frequency, which is shown through the simple regression below:

$$\mathrm{RANGE}_{ij} = \beta_0 + \beta_1 \mathrm{PFREQ}_i + \beta_2 \mathrm{AWP}_i + \beta_3 \mathrm{BR1}_i + \beta_4 \mathrm{BR2}_i + \beta_5 \mathrm{NEWB}_i + \sum_{k=6}^{25} \beta_k D_{ik} + \epsilon_{ij}. \quad (1)$$

The dependent variable in this model is RANGE_{ij} which represent price range across pharmacies in town *j* and it is the variable being studied in this model. While, PFREQ_i

- AWP is drug's acquisition cost.
- BR1 and BR2 are dummies for two kinds of brand-name drugs: those that face competition from generic equivalents and those that do not
- NEWB is a dummy variable for Newburgh
- *D* variables are indicators for 20 categories of drug therapy, which are included as crude controls

From the findings, measures of absolute dispersion and price-cost margins show a negative, statistically significant relationship with the prescription's purchase frequency Also, it was suggested by the researcher that even though, pharmacy differences explain roughly one-third of the price variation, price patterns are not consistent with a strict differentiated products story. The price dispersion is related to consumer search, which implies policies affecting the costs of acquiring price information; if dispersion is caused by imperfect information or policies that centralised price information, it may cause lower prices for consumers.