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Sorensen - Prescription drug

Equilibrium price dispersion in retail markets for prescription drugs

This article done by Alan T. Sorensen tries to establish the empirical importance of price dispersion due to costly consumer search by examining retail prices for prescription drugs. The study shows that search intensity , may be because lower marginal cost of price-shopping, has a negative relationship with price dispersion in this industry. If consumers become repeat purchasers of the drug, the propensity to search for low cost ones will be lower leading to lower search cost. So the pharmacy's ability to set a higher price would be dropped. Besides consumers' search cost, pharmacy heterogeneity and cost heterogeneity are also considered as other alternative explanations aiming to clarify price dispersion for the drug. However, consumer search is the most valid because two alternative explanations cannot fully explained. This study uses data collected from pharmacies located in Newburgh and Middletown. The interesting fact is that the price of prescription drugs vary in wide range of price even in the same area. The extent to which price dispersion is related to consumer search has important implications for policies affecting the costs of acquiring price information. Thus the absence of advertising or available information may result in higher price and much more price dispersion.

The Regression on Dispersion using model in Figure A) giving that the dependent variable is the price range. The estimates are obtained using GLS shown that there is only purchase frequency (PFREQ) that is statistically significant and has a negative coefficient. The importance of search models is that measures of margins and absolute dispersion should move together in response to changes in the search environment. From the result of dispersion and margin regression indicating that both margins and dispersion decline with a prescription's frequency of purchase.