TIERED PRICES
(or Differentiated Prices
or Market Segmentation)

What is it?

- A strategic use of price differentiation based on customers' wealth (irrespective of volumes purchased) in a system agreed upon by the global society, including the political power and social security institutions.
WHY ARE TIERED PRICES ECONOMICALLY FEASIBLE

If we look at what the cost of a product is composed of:

1) The most tiny part (often < 15%) is represented by the variable costs:

- raw materials
- packaging
- variable utilities
- direct labor
- container
WHY ARE TIERED PRICES ECONOMICALLY FEASIBLE

The essence of the cost is represented by non variable costs:

- **Fixed production costs:**
  - Staff
  - Supervision
  - QC / QA
  - Industrial planning
  - Industrial engineering
  - Industrial site management
  - Site utilities
  - Maintenance
  - Depreciation

- **R & D**

- **Administration costs**
  - Marketing & selling
  - Administration
  - And

- **The Profit**
THESE NON VARIABLE COSTS (INCLUDING PROFITS) CAN BE ARBITRARILY ALLOCATED, WHICH EXPLAINS THE PRICING FLEXIBILITY.
N.B.

1) This evolution in the ratio direct / indirect costs is one of the characteristics of modern economies

2) This trend would still be more important if we were considering distribution costs and taxes
Direct Costs

Indirect Costs of Production (fixed)

Administrative & Marketing Costs

R & D

PROFIT
Industrial Countries

Direct Costs

Indirect Costs of Production (Fixed)

Administrative & Marketing Costs

R & D

Profit
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**Diagram Description:**
- The diagram illustrates the cost structure for both industrial and developing countries.
- Direct costs are shown in red, indirect costs of production (fixed) in blue, administrative & marketing costs in yellow, and R & D in green.
- The profit is represented in purple.
- The bars for each country category are divided among the cost components as shown.

**Cost Breakdown:**
- Industrial Countries:
  - Direct Costs
  - Indirect Costs of Production (fixed)
  - Administrative & Marketing Costs
  - R & D
  - Profit
- Developing Countries:
  - Direct Costs
  - Indirect Costs of Production (Fixed)
FOR A COMPANY, IT IS POSSIBLE TO A LARGE EXTENT, TO IMPROVE THE GLOBAL PROFITABILITY IN SELLING ADDITIONAL QUANTITIES OF VACCINES AT A PRICE LESS THAN THE «FULLY LOADED COST»
THE FINANCIAL LIMITS OF THE SYSTEM

➢ Tiered prices have to rely on the existence of a solid market in industrial countries.

➢ These principles can apply if and when free production capacities do exist.

➢ In all other cases, where building up a new production capacity is necessary, the decision making process is subject to the regular allocation of resources.

➢ And the profitability is generated only when the financial and opportunity costs and depreciation are covered.
THE POLITICAL LIMITS OF THE SYSTEM

- Rich countries have to accept strong price differences (sense of excessive price)
- This problem is particularly acute when there is a monopoly situation
- Emerging economy countries have difficulties to accept intermediate prices (tendering system - PAHO)
THE PRACTICAL LIMITS OF THE SYSTEM

- Risk of parallel imports
- Coexistence in a country of two market segments at very tiered prices
CAN WE AFFORD NOT TO HAVE TIERED PRICES

- Without strongly tiered prices low-income countries will not have access to new products
  * They could not pay
  * Nor would third party payers be willing to pay

(Example of the conjugate pneumo vaccine)
CONJUGATE PNEUMO VACCINE

- 1.2 million children die every year in developing countries from a pneumococcus infection.
- Number of births in countries eligible to the Global Fund for Children Vaccines: 90 Million (including India and China).
- Number of doses necessary for a full immunization course: 3 + 1 Booster = 4 DOSES.
- U.S. Price per dose: U.S.$ 58.
- Total budget necessary: 58 $ x 4 doses x 90 M. children = U.S.$ 20.88 Billion.
CAN WE AFFORD NOT TO HAVE TIERED PRICES

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    (Example of the conjugate pneumo vaccine)

- Tiered prices are a trade-off between value and values
- They contribute to generating more equity
- Tiered prices represent an important mean of justifying intellectual property (indispensable to product development) in a context of limited access to therapy and prevention.
When Tiered Prices are put in place, other responsibilities will appear more clearly:

- For the rich countries, to help finance the acquisition of products.
- For the developing countries, develop the appropriate infrastructure.
- For all of us: to make the right priorities.