Pharmaceutical Group

16th January, 2003

Dear Sir,

In commenting on the draft report, we would like to make the general observation that it fails to recognise the importance of local industry, concentrating largely on issues from a multinational enterprise viewpoint. **(Commercial-in-confidence material omitted).** Combined with other PIIP participants such as Mayne, then clearly the local industry is a major source of value creation from pharmaceutical activities.

For local companies the business paradigm and decision-making is simple and clear. Our ability to invest in R & D and plant and equipment is directly linked to the margins that we can generate which depend in turn on the price and volume we can achieve in selling our products. Any significant degree of suppression in either of these parameters has therefore a major impact on our ability to grow our business, invest in R & D and create a virtuous cycle of investment and reward.

Turning to the detail of the report we would like to comment specifically on three areas.

1. Rationale for PIIP

We believe there remain a clear and credible rationale for PIIP in that significant price suppression continues to occur for our two largest PBS items. **(Commercial-in-confidence material omitted).** In addition there is no volume offset as suggested in the report. **(Commercial-in-confidence material omitted).**

2. Effectiveness of PIIP

We feel the assessment of the effectiveness of the scheme is too narrowly based in that it fails to acknowledge the long lead times in the industry and the effects of the previous factor f scheme in inducing activity over more than a decade. A good example of this is our collaboration with the University of Queensland and Merck in developing a vaccine to prevent HPV infection. Research conducted in the early 90's at the time of factor f is just reaching its final stages with the commencement of Phase III studies recently.

For CSL, who have been a participant in both schemes since 1990, the effect has been to enable us to sustain a **[higher**] level of R & D spend compared to the pre factor f level **(Commercial-in-confidence material omitted).**. In this respect, a shortcoming of the report is the failure to address the question, **'what would have happened to this activity in the absence of such a scheme?'**

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The wording of the findings (5.1) also do not adequately reflect that PIIP is one of the most effective government schemes across all industries for inducing activities especially R & D. Given the extent of price suppression, the level of compensation provided by the scheme is remarkably low for the activity it has generated. Our conclusion therefore is that PIIP has been highly effective.

3. Economic Efficiency of PIIP

We question the commission's conclusion that for local companies there is a negative net social benefit. The methodology employed appears to discount the large impact of PIIP on net exports of pharmaceuticals, its effect on the real exchange rate, and the possibility of substantial economy wide effects.

Looking to the future, our belief is that the rationale for a future scheme is as strong today as it was at the time of the inception of factor f. It is important that government continues to signal its conviction that it wants a viable domestic industry as enshrined in its National Medicinal Drug Policy. The design of a future scheme should retain the existing notions of being competitive and capped. Entitlements could be calculated on R & D activity above a base (possibly set at 3% of turnover) and for high value PVA such as the manufacturing of actives rather than packaging.

I trust these comments are helpful and look forward to publication of the final report.

Yours faithfully,

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PRESIDENT

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