

HKUST ECON Seminar

20 April, 2026, 3:00 – 4:30 pm

Contracting on Price, Compensating on Quality:

Evidence from Centralized Drug Procurement

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Abstract:

Centralized procurement sharply lowers drug prices, but competitive pressure may incentivize quality deterioration--a moral hazard problem with large welfare consequences. Using China's national drug procurement rollout and universal hospital transaction data, we document this quality-price tradeoff. Bid-winning firms are more likely to change manufacturing processes post-award, some consistent with quality reduction. Hospitals with the winning supplier altering packaging materials exhibit greater utilization increases, suggesting compensatory dosing. Prior branded-drug users resist switching to winning generics but use higher doses when switching. Accounting for compensatory dosing, the effective price reduction is 3--18 percentage points smaller than the nominal price cut.