strategy+business

ISSUE 66 SPRING 2012

The Faster New World of Healthcare

Regulatory reform and IT advances are accelerating the "clockspeed" in healthcare. To compete, insurers will need to focus on three key areas.

BY CARL DUMONT, ASHISH KAURA, AND

SUNDAR SUBRAMANIAN

REPRINT 00097

This article was originally published by Booz & Company.

pwc strategy& Formerly Booz & Company

The Faster New World of Healthcare

Regulatory reform and IT advances are accelerating the "clockspeed" in healthcare. To compete, insurers will need to focus on three key areas.

by Carl Dumont, Ashish Kaura, and Sundar Subramanian

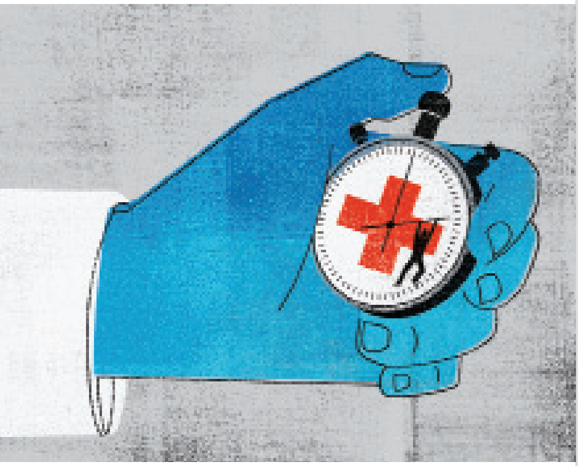
The healthcare industry in the U.S. is on the brink of unprecedented change. Wide-scale reform, a response to soaring costs and increasing demand, is forcing healthcare providers and insurers to rethink their value propositions and business models. It is also stimulating an equally unprecedented investment in IT. The health IT market is expected to experience a compound annual growth rate of 24 percent through 2014, according to RNCOS, a market research company. This overdue investment in IT is aimed squarely at the construction of a long-anticipated information backbone that will support improved care quality and cost reduction through enhanced connectivity and data analysis. (For more on improving healthcare, see "Health Reform by the Numbers," by GE Healthcare CEO John Dineen, *s+b*, Spring 2012.)

The developing health IT infrastructure, with its host of new applications, is ushering in the most intensely competitive era in the healthcare industry's history, by sharply accelerating the industry's *clockspeed*. Charles H. Fine of MIT's Sloan School of Management used the term to describe the pace of business evolution within industries. He found that industries with faster clockspeeds, such as computers and entertainment, had higher levels of market experimentation, more competition, and increasingly frequent waves of innovation. This will be challenging for the healthcare industry, and for insurers in particular, who are used to a much slower pace of change. To succeed, they'll need to look outside their sector for effective business models, and build new capabilities that support rapid product development, a consumer product mind-set, and expansion into adjacent markets.

Healthcare's Challenge

The leading healthcare insurers will find that IT modernization will either expand their role as information aggregators — making them the primary engine for higher-quality, more cost-effective care — or enable new competitors to supplant them. Historically, insurers have not needed a strategy for responding in a fast-paced environment. Repeated waves of consolidation (which oriented insurers toward scale rather than innovation), complex regulatory requirements that varied by market, the competing incentives and targets of multiple stakeholders, and the slow adoption of information standards have created speed bumps that impeded innovation. The ambiguity in healthcare reform's implementation may seem yet another reason for insurers to assume that the historical pace of the industry will continue.

However, as health IT becomes more connected, precise, and prevalent, many companies will have to race to realize its potential. Insurers' products have already begun to be



seen as commodities in the more consumer-driven post-reform marketplace, where health-insurance exchanges, bundled offerings, greater transparency, easy comparison of features, and lower switching costs will soon be commonplace. Add in the conditions typical in fast-clockspeed industries, and incumbents and even first movers could suffer competitive erosion, especially when new players and fast followers with deeper capabilities and more flexibility enter their markets.

For instance, greater granularity in claims data and significant investments in electronic health records (EHRs) will provide the raw material for improved analytics and will presumably lead to better medical outcomes. And these data sources are only part of the picture: More sophisticated medical devices and the ubiquity of social media and smartphones will enable faster, more comprehensive data collection and more effective interventions. Existing competitors and new entrants will create real-time decision support tools to help providers and patients better manage care. Microsoft, for example, is exploring virtual care delivery, and medical device manufacturer Medtronic has developed Wi-Fi-enabled cardiac devices that allow doctors to remotely monitor and assist patients. Insurers, who currently control claims data and the valuable insights contained therein, will face a crucial point of reinvention as these advances and the companies that field them engage consumers, influence medical utilization, and seek a proportional share of the healthcare dollar.

The Amazon Way

Health insurers looking for guidance on how to compete in a fast-paced environment won't find many examples within their own industry. But they can look to industries where the clockspeed has long been fast and furious, such as online retailing. One excellent model for them to study is Amazon.com Inc.

Amazon has built a full-service, seamless vertical approach — including order fulfillment, recommendations, and customer service — around its core retail business over the past decade. Simultaneously, it has staked out beachheads in key horizontal platforms, becoming a partner to other vendors through Amazon Marketplace, e-commerce hosting, and Web services (home of its much-ballyhooed cloud computing business). These businesses generate additional revenues that are funneled back into R&D for Amazon's core business.

This kind of approach could translate very well for healthcare insurers today, but to make it work, they will have to establish the proper balance between vertical and horizontal integration, and between control and speed. They will need a vertically integrated approach that keeps critical components under proprietary control to create differentiation. At the same time, they will need strong horizontal capabilities that can be deployed in fast and flexible ways to help master accelerating product cycles.

For example, insurers that decide to help physicians use EHR data will need swift application-development capabilities. That robust expertise could be deployed in multiple vehicles (such as cloud-based computing to the physician's desktop or to handheld devices) and for multiple purposes (for example, health analysis or prevention campaigns). New businesses like these could enable insurers to strengthen physician relationships and create future revenue streams. Amazon's example also suggests that the most successful insurers will be those that continually engage their customers through product design and nimbly capitalize on emerging capabilities.

Three Areas of Focus

To compete effectively in a faster environment, insurers will need to develop capabilities that enable them to achieve the following outcomes.

1. Business systems designed for rapid product development. Insurers often serve several customer segments in different regions and provider networks. This emphasis on breadth has contributed to an abundance of uncoordinated technology strategies and a scattershot approach to value chain design. Furthermore, speed-to-market has often

Illustration by Keith Negley

been achieved via custom development rather than via an architecture designed for rapid product cycles. Over the long term, this hampers insurers' efforts to be truly nimble.

Insurers need a coherent infrastructure that can deliver over successive product cycles. This suggests that they should adopt a business architecture that can be broken into simpler subsystems, that uses modular and off-the-shelf components, that assumes technological obsolescence, and that preserves future flexibility.

2. A consumer product design mind-set. Insurers have traditionally maintained market share by locking in networks of customers and providers, and in many markets by relying on strong brand names. But they may be ill-equipped to compete on product features in an environment with low switching costs and intense competition.

To succeed in this emerging environment, successful health plans will develop robust product ideation and iteration capabilities. They will use these capabilities to better align demand with care utilization, creating new products (such as one-price care bundles) and designing incentives that shift care to less-expensive channels (such as non-acute care facilities and preventive health programs). In addition, to capture the expected growth in individual and small group markets, insurers will need to sell directly to these groups, manage their experience, and encourage healthy behaviors. This will require new retail capabilities in customer engagement, including the support and provision of enhanced interventions and self-care, as well as new service channels.

3. Expertise in entering adjacent markets. Although some insurers may decide to stick to their traditional strengths in core administrative services to insulate them from the faster pace, they are likely to discover that competing on transactions alone has drawbacks. The large-scale system migrations required to significantly improve transaction speeds are both costly and risky. Only a few insurers will achieve the necessary economies of scale, and they will most likely become outsourcing partners for the rest of the industry.

Instead, most insurers should be looking for areas where there is headroom for growth, such as adjacent markets for care delivery. Because clinical care delivery accounts for almost 80 cents of every healthcare dollar spent in the U.S., products and services aimed at delivering more effective outcomes at lower costs, solving ambiguous clinical problems, and promoting virtual care delivery are rich areas of new opportunity for health plans. Successful plans will consolidate a broad range of platforms, including smartphones, cloud-based computing, and videoconferencing, to launch care products that deliver greater value. They will also master the art of relationship building and creative collaboration to overcome adversarial provider relationships and consumer mistrust.

Keeping Pace with Change

Insurers will succeed either by meeting multiple needs within their chosen markets or by realizing the full breadth of capabilities in their horizontal niches; over time, they may do both. In any of these scenarios, however, health insurers will have to design value chains that can deliver successive waves of innovation. They must be prepared to quickly generate and launch new products and services, learn, adapt, and repeat the process, if they hope to profitably retain fickle customers who traditionally have not taken a great deal of responsibility for or control over their own care. Clearly, existing players won't be able to depend on their hard-won brand equity. In other industries, established brand names have meant little when the pace of innovation has accelerated (think of Encyclopedia Britannica, displaced by Wikipedia's open source model). As Charles Fine's work on clockspeed ultimately concluded, the only enduring competitive advantage is the ability to continuously assess and build value chains that exploit current opportunities and anticipate future ones. +

Successful health plans will master the art of creative collaboration to overcome consumer mistrust.

Reprint No. 00097

Carl Dumont
carl.dumont@booz.com
is a partner in Booz & Company's global healthcare practice based in New York.

Ashish Kaura
ashish.kaura@booz.com
is a partner in Booz & Company's global healthcare practice based in Chicago.

Sundar Subramanian
sundar.subramanian@booz.com
is a principal in Booz & Company's global healthcare and operations practices based in New York.

strategy+business magazine
is published by PwC Strategy& Inc.
To subscribe, visit strategy-business.com
or call 1-855-869-4862.

For more information about Strategy&,
visit www.strategyand.pwc.com

• strategy-business.com
• facebook.com/strategybusiness
• http://twitter.com/stratandbiz
101 Park Ave., 18th Floor, New York, NY 10178

pwc | strategy&
Formerly Booz & Company