

# Briefs

## A Trillion-Dollar Opportunity

A revolution in the way companies provide health-care benefits is poised to trigger a convergence of health-care and financial services, and crack open a \$1 trillion opportunity for U.S. financial-services providers by 2010. In the process, millions of new individual investment accounts will be created.

As we wrote last year in *strategy+business* (see “Health Care’s New Electronic Marketplace,” Second Quarter 2000), the forces that redrew the retirement-savings scene in the 1980s are at work again. Just as corporate pension plans were supplanted by 401(k) plans directed by individual consumers and managed by financial-services providers, so could consumer-directed health-care accounts soon become the norm.

E-commerce innovation and new players in the health insurance arena will lead the way. We envision a defined-contribution model built around Web sites where employees make choices using a voucher or specified amount of pretax employer dollars, with options to increase coverage or plan features with their

own pretax funds. Firms like Definity Health and SimplyHealth already have retail portals where employees can select coverage, networks, and critical health-plan features.

Now contemplate the bulk of the nation’s total health-care expenditures in 2001 (estimated by the Health Care Financing Administration at \$1.4 trillion and expected to grow to \$2.4 trillion by 2010) flowing into individually held retail investment accounts. Who is going to aggregate and manage the staggering floats involved, let alone the accumulated and invested rollover balances?

Because health-care benefit dollars historically have been managed by employers, they are separated from the consumer banking and investment system. Defined-contribution health-care programs will change that by putting these sums into individual self-managed accounts serving short- and long-term health-care financing needs.

Defined-contribution health-care plans have the potential to create 50 to 100 million new individual accounts, giving financial-services firms the opportunity to pursue lucrative aggregation and cross-selling strategies. No new

money will be created per se, but an enormous shift will occur that moves \$1 trillion a year from corporate checking accounts and institutional insurance pools into personal banking and investment accounts. Smart financial-services providers already are building strategies to integrate lifelong funding for health-care risk with retirement funding, then linking them with routine retail banking services.

Imagine a single online enterprise offering total money and benefit management for consumers. A consumer’s paycheck might go directly to this enterprise, which would buy or administer retirement and health-care benefits. The same service could provide online checking, credit cards, mortgages, and other types of insurance, too. The revenue potential for such service providers is huge, and the customer’s experience would be better and simpler.

Already thinking along these lines, Halifax PLC, one of Britain’s well-known retail financial-services brands, is marketing Intelligent Finance (IF), a Web- and telephone-based money-management service. The IF plan finds daily the best net interest position for a customer’s

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mix of debt (e.g., credit card, mortgage) and assets (e.g., savings, checking), allowing consumers to either maximize the interest on their savings or minimize the interest on their borrowings.

Potential leaders and players are most likely to come from the banking and investment world rather than the health-insurance industry or the e-commerce infrastructure field. That's because a retail focus will be key — and the investment community's experience over the past decade with individual retirement vehicles has created some of the infrastructure and customer-service orientation that will be needed. Whoever steps in to lead the convergence, it's clear that businesses will not let America's \$1 trillion float go unmanaged.

**Gary Ahlquist, David G. Knott, and  
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## How Organizational Aging Affects Innovation

When a company is threatened by an innovative technology, should it rush to embrace and develop it? Not necessarily. The organizational

response to innovation changes as a company ages. Older companies tend to be better at incremental innovation — developing products from an existing patent portfolio or knowledge base. But as a company matures, it loses much of its ability to respond directly to rapid and radical innovations. Aging companies must assess their capabilities *before* reacting to market disruptions.

Established firms excel at wringing new product lines and line extensions from existing assets, and selling into markets pioneered by others. They are more efficient at creating patent portfolios, for example, that can protect new product lines and create future licensing revenues. They also have existing distribution channels and marketing relationships that help get products into customers' hands quickly. Diversified companies can combine the skills and technology of different operations. The Sharp Electronics Corporation, for example, invests a third of its R&D projects across divisional lines. This approach led to Sharp's development of handheld devices that use the Microsoft Windows CE operating system.

However, older companies' organizational factors — such as

bureaucracy, poor communication among divisions, work forces that don't have the skills or knowledge to respond to new opportunities, and inflexible resource allocations — inhibit fast responses to radical innovations. In the early 1990s, for instance, combinatorial chemistry transformed drug discovery from a labor-intensive process to a computerized exploration of molecular compounds. Startups became the pioneers in this area, but big pharmaceutical companies couldn't pounce on the opportunity, in part because synthetic chemists felt threatened by the new technology. Politics prevented the allocation of significant resources to this new research, which made it difficult for big pharmaceutical companies to recruit combinatorial chemists with leading-edge knowledge.

Established companies have pursued expensive, distracting strategies, such as skunkworks and corporate venturing, to become as nimble as startups. But in many cases, the operations either failed to innovate or could not capitalize on their breakthroughs. Similarly, the Xerox Corporation for years did not capture value from such innovations as graphic user interfaces and laser

printers developed at its Palo Alto Research Center.

Nevertheless, older firms can use their wisdom and age to trump speed and youth if they:

- **Remain patient.** Startups, backed by impatient venture capitalists, feel pressure to rush their innovations to market; older companies can wait for evidence of long-term disruptive effects. In e-tailing, this scenario has played out repeatedly: First-movers established technology standards and market visibility, but couldn't generate profits. The Webvan Group Inc., incorporated in 1996, spent \$1.2 billion to build grocery delivery services to households in the United States before going out of business this year. Royal Ahold, the Dutch owner of Stop & Shop and other grocery chains, waited until 2000 before acquiring a majority stake in e-grocer Peapod Inc., and has since acquired the entire company, all for

less than 10 percent of Webvan's lifetime losses. Royal Ahold already had the brand and infrastructure to support an online operation. Now it benefits from others' investments in refining tools for e-commerce site construction, a glut of technology workers, a larger base of online consumers, and accepted standards for online customer service.

- **Ally or buy.** Alliances or acquisitions give older companies the chance to become players. Eli Lilly and Company, for example, bought its way into combinatorial chemistry with its 1994 acquisition of the Sphinx Pharmaceuticals Corporation. By then the technology had proved its value for drug discovery.

- **Use existing strengths.** Some companies, like the Sony Corporation, create disruptive technologies, whereas others are technological followers that compete on their distribution and marketing prowess and other resources. Sony's

rival in consumer electronics, Matsushita Electric Industrial Company, has built its Panasonic brand through its sales operations and advertising, rather than technological innovation.

Aging is a fact of life, and companies need to assess their strengths, weaknesses, and options honestly before responding to external changes. Clearly, aging companies can benefit from disruptive technologies, but their responses don't have to be, and should not be, the same as those of younger companies.

**Toby E. Stuart**

## Global Best

## Practices Meet

## Local Realities

Companies often use enterprise resource planning (ERP) and knowledge management (KM) systems to facilitate company-wide business process improvement and innovation. They mine, analyze, and package global best practices in ERP and KM databases, thinking it will be easy and efficient to share the information across their organization. It's not. Best practices almost always have to be adapted to local conditions, and data captured in ERP and KM systems rarely reflect these nuances. What's usually missing? Human interpretation.

For example, a global clothing manufacturer's Italian subsidiary adopted an ERP system's human resources module, which required automated recruiting and selection procedures. But this proved counterproductive; informal, in-person recruiting worked best in the region. Recruiting performance actually declined until the automated parts of the new module were bypassed

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and personal interviewing was revived.

KM systems also fail to deliver value when their best practices are accepted without a human being's critical judgment. An international bank introduced a KM system as a source of standard global solutions for customer-service problems. One department, seeking to quicken mortgage application processing, adopted a best practice — electronic mortgage applications — that had worked well in another country. The problem was, most of its customers didn't have Internet access, so customer complaints about the application process increased.

In each of these cases, managers assumed the ERP and KM systems held all the answers, and they did not bother to confer with colleagues working with similar problems and circumstances. Had they used the systems as brainstorming tools, rather than blanket solutions, the benefits of having a database of global best practices to augment their local knowledge might have been much greater.

ERP and KM should be seen for what they are, data-processing systems that capture information: ERP for business processes (e.g., documenting process flow and procedures); KM for ideas (e.g., capturing and transferring specific expertise). Such systems efficiently collect and transfer data, but don't make sense of it. It's up to managers to interpret and modify data in each new context.

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