

February 2018 Newsletter

Would you bet against Jeff Bezos, Warren Buffett and Jamie Dimon?
The shock wave felt across the health care business

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Dear Colleagues,

As it happens, I was at Magellan Healthcare's **MOVE conference** when the news hit that these three movers and shakers have agreed to form a new company to do something about burgeoning costs and other problems in the healthcare business. While the details are still unclear, the agreement has a lot of people in the healthcare system wondering what it might mean for them.

The hungry tapeworm of ballooning healthcare costs

Warren Buffett is ever brilliant at a turn of phrase, and this one is no different. Not only are healthcare costs in the United States higher than they are in the rest of the world, they've also been rising faster than elsewhere. According to *Consumer Reports*, if you sliced out healthcare spending in the United States and made a country out of it, it would be the world's fifth largest economy.

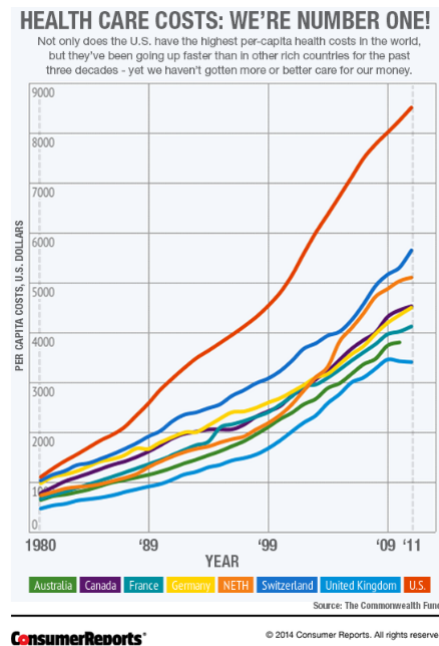
The negative consequences of one sector sucking up so much of the economy are, indeed, dire. Funds going into healthcare aren't available for other things – things like raises for workers, for instance, contributing to flat wages and limited earning power for many. The Bezos-Buffett-Dimon agreement clearly signals that the frustration with seemingly intractable momentum in rising costs has reached some kind of tipping point.

Completely broken market mechanisms

According to Capitalism 101, prices for things are set by market mechanisms. Buyers try to get the lowest prices they can get, and sellers try to get the highest, and depending on the laws of supply and demand they eventually negotiate a deal. Not so with healthcare. Indeed, the former CEO of Kaiser Permanente a massive health maintenance organization based in California, George Halvorson, observed, “Prices are made up depending on who the payer is.”

Further, because the delivery of healthcare is fragmented across all kinds of providers, system-wide savings do not necessarily benefit any given player. For instance, investing in preventive care (which costs something up front) may save the cost of looking after severe, untreated conditions down the road (which is generally more expensive). But the cost is borne by a different party than reaps the benefit of the savings, so the incentives are mis-aligned. We're beginning to see the consequences of this with the broad adoption of high deductible health plans (HDHP's) in which consumers are responsible for more of their own costs.

While the logic behind HDHP's was that they would incent consumers to shop more intelligently for their care, this hasn't necessarily happened. Patients are skipping medications and treatments to save cost. In a recent tragic case, Heather Holland, a second-grade teacher, died of the flu after deciding to skip a medication (costing \$116) that might have saved her



life. The Kaiser Family Foundation said this isn't unusual, reporting that 43% of insured patients skipped a recommended test or treatment due to **high costs**. Healthcare providers are feeling the strain as well – hospitals are reporting sharp increases in unpaid collectibles from patients who are unable to afford the larger portion of the cost of their care with these plans.

Miracle cures – but at a price

On the pharmaceutical side of the business, the industry continues to produce cures that for the people affected are miraculous. Sovaldi actually cures Hepatitis C, in many cases preventing the need for liver transplants that can cost up to \$500,000. The price of the drug? A course can run \$84,000 to \$150,000. Remicade, a treatment for diseases as varied as arthritis and Crohn's is pricey as well, although finding an exact number is a challenge. Sources report costs of anywhere from \$3,000 to \$13,000 per treatment for a drug that is administered every six weeks.



Another cost-inflating practice became a major scandal, when drug company executives realized that they could acquire older drugs (that they made no investment to develop) and use favorable market positions to jack the prices up astronomically. Essentially, absent a market mechanism, the justification for this on the part of these executives was “because I can”. **Four companies** were considered to be so egregious in their practices that the Senate

Aging Committee investigated them - Turing Pharmaceuticals, Retrophin Inc., Valeant Pharmaceuticals International and Rodelis Therapeutics. Among their findings:

- The price increases had nothing to do with creating new treatments and everything to do with rewarding investors and executives at the companies;
- The companies deliberately withheld supplies of the drugs from competitors so that the competition couldn't prove it could make the same thing;
- Programs to help patients with co-pays basically ended up sticking insurance companies with vastly larger bills than they previously had, raising costs for everyone in the system.

It's hardly surprising that legislators and policymakers are starting to consider **taking action** against these practices.

Perverse incentives and the shift to paying for value?

Further, the piecemeal delivery of most healthcare services in the U.S. creates incentives to do more, not less, even if the service is not, strictly speaking, necessary. Unlike other industries, in which increased efficiency makes an



organization more competitive, efficiency in healthcare delivery means less revenue. Innovating to require one CT scan rather than three, for instance, means a provider only gets paid once, not three times.

To better align incentives with rewards, many players in the ecosystem have concluded that a payment system based on value – on patient outcomes, for instance – rather than activities makes more sense. If a group made less money, not more, by operating inefficiently, the incentive to do so would diminish. The unintended consequence of course, is that with the incentives now heading in the opposite direction, there may well be a reward for withholding necessary or expensive care from patients. Or of **rationing care**, which is already common practice in countries with single-payer systems. Indeed, the United States differs from most other countries where effectiveness calculations are used to determine who has access to care. The result in many places is indeed, rationing. The sad reality, of course is that the US is no different than any other place in the sense that only so much can be spent on healthcare, and so some form of rationing is inevitable.

So what innovations might the new healthcare company pursue?

Let's call this new entity HealthCo. What might it do to try to rein in healthcare costs? To make an impact, HealthCo is going to have to try to tame the fragmentation in the current delivery system so that savings in one part of the system benefit the whole. One likely effort is to cut out the middlemen involved in the distribution of pharmaceuticals and other medical supplies. Companies such as Amerisource, Cardinal Health and McKesson could see themselves disintermediated in a big way.

A second group that could find themselves in HealthCo's sights are Pharmacy Benefit Managers (PBM's) such as Express Scripts Holding, OptumRx (a unit of insurer UnitedHealth Group), and CVS Health. These few companies "process about 70 percent of the nation's prescriptions, according to Pembroke Consulting". The experience of companies like Caterpillar who have **cut out the PBM's** by hiring its own doctors and pharmacists is an illustrative tale of how effective an alternative

own doctors and pharmacists is an illustrative tale of how effective an alternative model can be. According to a recent analysis, \$15 of every \$100 spent on brand-name pharmaceuticals goes to middlemen, as opposed to about \$4 of that \$100 that



is spent in other countries. In a clear indication that standard PBM practices are not necessarily in their customers' interests, the industry has strongly resisted being held to a fiduciary standard (in which they would have to bear the best interests of their customers in mind as they make recommendations), and smaller, more transparent PBM's than the large ones show savings of 15% or more as compared to the large incumbents.

Given the size of HealthCo's potential covered base of employees, it could negotiate directly with pharmaceutical firms or even force them to bid on the right to supply certain types of solutions. As one of the participants in the Magellan MOVE conference observed, one outcome could have the effect of single payer pricing, as prices offered to HealthCo would set a standard for prices offered to everybody else.

The big problem with paying for healthcare, unlike other forms of insurance, is that there is no uncertainty about people's need to use it. We are all born, suffer from maladies, and die. In other words, we know there will be spending involved on the part of whoever is paying for care. That is a context in which the U.S. system of for-profit players, itself a historical accident, makes less and less sense.

Women in Technology - A Columbia conference

I was delighted on February 9 to be part of the Columbia conference *Women Business Leadership in Technology: From Talk to Action*. The event was sponsored by **Robert Smith**, the Founder and CEO of Vista Equity Partners. The event brought together senior leaders in technology firms, Columbia faculty and students and alumni to promote the idea that women can and should take leading roles in technology enterprises (and who isn't a technology enterprise these days?).

Among the sound bites:

- Women don't delegate as much as they should / could – they feel better about it if delegation is framed in terms of increasing skill and bringing younger people along.
 - Delegate, don't abdicate.
 - Women who are stalled, probably didn't take enough risk early on.
 - Life is too short to work with jerks.
 - Older founders start with the problems from their own lives – diversifying the issues that get startup attention – for example finding ways to make it easier to care for older people.
 - “I thought I must not be as sharp as they were, then I realized, they're not so smart, they're basic white guys (BWG's) and I'm as good as any of them.”
 - If you want diversity, start early. It's easier to add the first female engineer when she is one of 5 than when she is one of 500.
 - When women have more power, gender differences are diminished.
 - Not all bias is unconscious!
 - A new trend in careers is that women in their 50's can have a real flourishing – calls into question the ratchet of traditional career paths.
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Women of Color in Pharma (WOCIP)

On January 16, I was the keynote speaker for a conference sponsored by **Women of Color in Pharma** (WOCIP). Entirely member-initiated and organically grown, WOCIP is creating genuine community, with this event's theme being “Don't Take It Personal”. The keynote covered some of the major trends affecting the pharmaceutical industry in general, including fewer blockbuster drugs, more stringent approval requirements and the industry-wide struggle to return its cost of capital. I then delved into how this can affect people's careers and made some suggestions on how you can create a more resilient career strategy for yourself.

That was followed by a vibrant panel discussion, moderated by **Trudy Bourgeois**, founder of the Center for Workforce Excellence and a true path-breaker. Among her accomplishments were to become the first African American woman to rise to the level of Vice President in a major consumer goods company. One of the panel highlights was from **Virginia Lazala**, Vice President and Section Head of the Legal Department at Novartis, who advised the people in the audience to “dream big and do you!”.

Upcoming Events -

Chris Rainey Podcast (February 20, 2018)

Chris Rainey and I will be doing an interview for his podcast with Human Resource Developers, an international community of Human Resource leaders. We will be talking about how talent management changes in a transient advantage context when people are employed in a “tour of duty” context and how the leadership of the Human Resource function needs to evolve.

Einstein's Alley - Future of Work Part 4 (March 5, 2018)

Leading Your Workforce in Uncertain Times
Featuring Rita Gunther McGrath and Ron Boire
March 5, 2018, 4:00 - 6:30 PM
Lawrenceville, New Jersey

This is a special opportunity as this event is open to the public. I'll be discussing the future of work as it relates to “**Talent Deployment in a Tour of Duty World.**”

We all know, the American workforce of the near future will look nothing like the American workforce of the recent past.

As the pace of change accelerates, the way you manage your most important resource – talent needs to change too. Join us as we discuss how best to motivate and incentivize people and how you may even change the way you think about 'human resources.'

You will also have the pleasure of learning from **Ron Boire**, who specializes in organizational transformation as he talks about “**The Human Touch in Executive Leadership**”.

Employees need to feel psychologically safe; they need to know that leaders value and respect them; and they need to believe that their work is meaningful and that

their ideas are heard. Creating an engaged and productive workforce requires trust, and trust is built over time, face to face. Boire will draw upon his extensive experience with organizational transformations to share his observations of what works, and what doesn't, in creating an engaged and productive workforce.

Join us for these informative talks as well as participate in facilitated group discussions followed by a networking Wine Reception.

[Watch Rita's recent interview for i-CIO Magazine.](#)

Join us in a highly interactive setting at [CoWork ConnectionPlus](#) in Lawrenceville, New Jersey.

[Register Today](#) and visit [Einstein's Alley](#) for more information.

Take advantage of the early bird rate through February 28, 2018.

HBR Facebook Live Session (March 30, 2018)

I'll once again be at *Harvard Business Review's* headquarters to lead a Facebook live session on my new work. While we haven't pinned the topic down completely, it is likely to feature some of my newer work on strategic inflection points. If you want to get a feel for what it will be like, check out my previous Facebook live session [here](#).

Digital Business Strategy (April 11 - 13, 2018)

I'll be joining my good friend and colleague, David Rogers, for a Columbia Business School Executive Education event that is part of our portfolio of digital development courses. David is the author of the *[Digital Transformation Playbook: How to Rethink Your Business for the Digital Age](#)* and together we help companies figure out where digital disruption might present opportunities. You can find out more about the course [here](#).

Leading Strategic Growth and Change (May 7 - 11, 2018)

Just a reminder that my [course on innovation](#) and growth will be running next in May of 2018. For this run, I'm delighted that we are going to be joined by [Future Partners](#) the "Think Wrong" company driving the next generation of design thinking. They will be working with our participants to learn how to apply the fast-paced and energizing properties of design thinking to the challenges they bring to the course, and I'm really looking forward to working with them. Also new for this edition is a business simulation of [discovery driven planning](#) which lets our participants experience the reality of the technique, not just read about it in a book. My co-author and colleague Alexander van Putten, a strategy consultant, will be with us to lead that.

Participants bring a real organizational challenge to the program and work on it throughout the week. Click [here](#) for more information. Or drop me a line at rdm20@gsb.columbia.edu.

Women in Leadership (June 5 - 8, 2018)

A timely and topical Columbia course is our own [Women in Leadership](#): Expanding Influence and Leading Change. At the June course, we will be joined by [Sally Helgesen](#) who is on the brink of publishing her co-authored book with Marshall Goldsmith *How Women Rise*, which will be hot off the presses at that point. Sally will be sharing her research showing how the practices that helped executive women as they began their careers, can become liabilities the further they advance. We will also be joined by Cindy Pace, an Assistant Vice President of MetLife who will share her [organization's journey](#) with respect to diversity and inclusion.

It isn't too early to start planning for the Drucker Forum's 10th Annual Meeting

An event I've really come to enjoy is the annual [Peter Drucker Forum](#), held in Vienna. Next year marks the 10th annual meeting, and it promises to be a star-studded event at the Vienna Imperial Palace on November 29 and 30, 2018. The conference theme will be

“Management; The Human Dimension.” If past events are any gauge, the speakers will be world-famous management thinkers and scholars. We’ve never needed Drucker’s wisdom more than now!

To get a flavor of the discussions at this year’s Forum, see this [excellent overview](#) by Steve Denning.

New Research

The March – April edition of *Strategy + Leadership* will feature some new research by myself, Alexander B. van Putten and Ron Pierantozzi (two colleagues with whom I have long worked in the area of strategic growth). In it, we describe how to judge the credibility of a company’s growth strategy with a measure we call *The Imagination Premium*™. While we can’t give it away pre-publication, let me just say that it explains some counter-intuitive movements in the stocks of Amazon, Walmart, Tesla and Buffalo Wild Wings. More on that after publication. If you’d like to learn more, please contact me at rdm20@columbia.edu.

Recent Articles and Press Coverage:

[Why are some industries hiring the most female CEO’s?](#) *Moneyish* talks to Rita McGrath.

My good friend and colleague, Melissa Schilling, has launched her new book on what constitutes true genius, called *Quirky*. You can read about it [here](#).

[How Amazon is transforming the grocery sector and what we might want to do about it.](#)

[Seven big ideas](#) from the Drucker Forum.

Steve Denning has also launched his groundbreaking book, *The Age of Agile*. It’s a manifesto for the rest of us. You can read about it [here](#).

As before, where there is uncertainty, there is also opportunity

We're going to be spending the next month laying the groundwork for the launch of a sister company to the Rita McGrath Group, Valize LLC. Valize is designed to help companies make discovery driven growth a reality by linking leading experts and time-tested innovation tools to benefit its clients. Watch this space for new developments!

Here's to your next advantage!

Rita

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