OLIVER WYMAN

Health & Life Sciences

Executive Briefing: The Four P's of Post-Reform, Part 2

Product Strategy: When Consumers Rule

For decades, "product design" has meant benefits and network. In the new world of retail healthcare, that won't be enough to attract and hold customers. Here's a new product model that will.

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Imagine: It is January 2014, and Jane Doe is shopping for health insurance. Jane, a 45-year-old mother of two, has been without coverage for five years, but that is about to change thanks to the Affordable Care Act and a generous subsidy from the federal government. All Jane needs to do is select a policy, and in the new world of consumer-oriented health insurance, she has a range of compelling choices that go far beyond the traditional selection of cost and network:

- Should Jane give up her current doctor and sign up for a patient-centered medical home and a predefined network in exchange for wellness benefits and no out-of-pocket costs?
- Or, given her current medical condition, would she be better off agreeing to proactively manage her diabetes and share lab results with her insurer in exchange for a healthcare coach, lower out-of-pocket costs, and a guarantee of no cost increase for the next year?
- Or, will she sign up for the patient-centered medical home, the health risk assessment, and consumer engagement programs in exchange for a two-year guarantee of no out-of-pocket costs and two years of term life insurance?

The individuals making up the new consumer market will have the power to reshape healthcare.

Jane and her choices matter, because she represents a powerful new cohort of consumers who will enter the individual insurance market between now and 2020, bringing with them enormous opportunities and the purchasing power needed to drive real change to health insurance. The bulk of them—we estimate 80 to 120 million consumers—will shop on the federally mandated exchanges, while others will turn to private exchanges, membership associations, and traditional brokers. Some of these consumers are currently uninsured; others will migrate from the small and large group markets. Some will pay their own premiums; others will be subsidized by employers or the government. Together, they promise to reshape health insurance from a relatively staid wholesale business to a dynamic consumer marketplace.

In Part One of "The Four P's of Post-Reform," we described a framework for understanding that marketplace. In Part Two, we turn in greater detail to the first of the P's, product design. This is an area where health plans need to rethink some of their most basic assumptions. Traditional health insurance products were designed for what is basically a wholesale market; they focus almost solely on the factors employers care about: price or cost, benefit design, and network

The Exchanges: Where Consumers Will Be

The new consumer healthcare marketplace will be centered on state and regional exchanges. Middle-of-the-road estimates show the exchanges serving 100 million consumers or more by 2020.

Existing exchanges, including the Massachusetts Connector and the Utah Health Exchange, serve only a handful of consumers

Between 2010 and 2015, the market grows by:

12-15 million previously uninsured

3-5 million moving from small groups

10-15 million former small group members buying coverage on the exchanges, either as group coverage or direct-contribution (DC) programs

10 million moving from the traditional individual market

Between 2015 and 2020, the exchanges add:

An additional **8-15 million** previously uninsured

2-5 million moving from small groups to the individual market

10-20 million more small-group employees buying group or DC coverage on the exchanges

20-30 million large group employees on DC plans

5 million from the individual market

Source: Oliver Wyman estimates.

model. They are not designed for a consumer-driven market, and they won't succeed there. It is time not just for new insurance products, but for a new product model.

Structured Choices, Compelling Options

Traditional health insurance, designed for what employers care about, will not succeed in a consumer-driven market. It's time for a new product model.

By product model, we mean a structured set of choices within a range of price points. Its goal is to allow different customer segments to focus their buying power on the elements of value that matter most to them. Oliver Wyman believes that in order to offer a meaningful array of choices across a range of price points and consumer segments, the new product model must include five integrated components. Within each component, depending on how reform is implemented on a state level, there will likely be opportunities for insurers to offer incentives for desirable behaviors, or to give customers the opportunity to "buy up" benefits or "buy down" costs.

- **Benefits:** Healthcare products, within the limits of federal and state regulations, will be able to offer varying levels of health benefits. But that is just the start of the variation possible within this component: Products may include options to increase health coverage or bundle it with non-health benefits such as life insurance or a health club membership.
- **Provider network model:** A key area where health plans can offer tradeoffs is in network models. Leading providers will reorganize their business models to compete on value, providing health plans with the option to offer value-priced products based on a locally branded Accountable Care Organization (ACO) or a series of centers of excellence for cardiology, oncology, and orthopedics. Health plans will have the opportunity to give consumers more choice—for example, a value-priced ACO model in exchange for increased benefits or lower out-of-pocket costs. Remember, it was the employers, not consumers, that drove one-size-fits-all, broad-access networks.
- **Medical homes:** Clearly, health plans with medical home networks should be able to offer consumers better overall benefit value through the medical home model—evidence-based, integrated treatment management, focus on reduction of health risk factors, care coordination, etc. The design of individual products may include incentives—a buy-up of benefits or a reduction of out-of-pocket costs—for patients who sign up to have their care coordinated through a medical home model. And consumer demand may increase competition between medical homes, resulting in better value for the buyer over time.

Innovative health plans will break functional silos and reflect the value of a new integrated product model in their pricing.

- **Health engagement models:** Again, it is not certain yet what will be allowed under the new system, but the new product model may allow consumers to enjoy a "good driving record" approach to health insurance. Under this sort of system, consumers could qualify for additional benefits or buy down premiums by proactively managing their health status and participating in health plan programs—completing a health risk assessment, building a health improvement plan, reducing risk factors over the course of the year, or successfully managing a chronic disease.
- **Service support**: Consumer service support needs will vary significantly across segments. Some self-directed consumers, perhaps with a medical home, will be delighted with an easy-to-use online service model and would love to subscribe to the model in exchange for a better price point. Other consumers will expect higher-touch service to be included—and others will pay a premium for à la carte services.

These components can be used to create a wide variety of innovative products fine-tuned to the needs of particular customer segments. Intuitive—yes; easy to do—no! Health plans moving to the new product model will have to integrate their value chains (breaking functional silos) and learn how to reflect the value of the new integrated product models in market-based pricing.

Two important notes: (1) The Affordable Care Act does not fully eliminate the disconnect between who pays for health benefits and who receives the care. The government will subsidize premiums for Americans at or below 400 percent of the Federal Poverty Level (FPL), and many consumers will pay for only a portion of their healthcare costs. Their buying decisions will therefore be made net of subsidies. Consumers or households with incomes at or near the FPL will receive significant subsidies and may select a healthcare option that minimizes out-of-pocket costs, while consumers with incomes between 350 to 400 percent of the FPL are likely to carefully balance what they want with what they can afford. The table, The Real Price—After Subsidies on page 5, illustrates consumer subsidy levels by household income and the corresponding premium costs for traditional plan designs. (2) We have approached the issue of product design with an eye toward winning and retaining consumers, but have largely ignored the strategy of risk attraction and risk arbitrage. While it is true that some companies may win short-term gains with such a strategy, we believe the mandated risk adjustment program in the Affordable Care Act will quickly render the strategy untenable.

Mapping the emerging consumer segmentation with the core components of a consumer-driven product design is a critical first step in product innovation.

The Real Price—After Subsidies

In the post-reform world, consumers will focus not just on the price of insurance, but the price after federal subsidies. This example shows what consumers in various income brackets would pay for an identical silver policy, priced at $576 a month for 60- to 64-year-olds (■) and $197 a month for 18- to 24-year-olds (■).

Oliver Wyman analysis

Understanding Consumer Buying Strategies

The new product model for health insurance, like any product model, demands detailed understanding of the customer and of customer segments. This is a job for market research, and Oliver Wyman is currently fielding a major study to examine what specific features consumers want in their health insurance and how they weight various components. The results of the study will be released later this fall.

But even without the benefit of the complete study, Oliver Wyman's past research on the individual market provides a starting perspective on basic consumer strategies for selecting health insurance.

The *active health value manager* wants the greatest access to quality healthcare for the lowest price. This consumer will select the appropriate benefit plan and then "buy down" the price by fully participating in health engagement programs, selecting a medical home, picking an all-in local market ACO, and subscribing for the self-service model. Depending on specific product designs, these choices might virtually eliminate out-of-pocket costs, guarantee a low renewal price, and allow the consumer to earn points towards a fitness club membership.

The *price shopper* is looking for the best in-year deal and may be willing to buy down benefits through higher deductibles. Some price shoppers, however, are likely to select a medical home and an integrated local network in order to reduce net costs. This transactional consumer may not elect to participate in the health engagement programs and would not be looking for a multi-year relationship.

The *partner for life* wants a stable, trust-based relationship with a health plan that meets consumer needs and offers one-stop shopping for a benefits portfolio that extends beyond health—life, STD/LTD, long-term care, etc. This consumer may be interested in a "frequent flyer" program with multi-year pricing and an incentive-accumulation system with a lifetime focused service model.

For an example of how these strategies can be mapped against the five components of the new product design to suggest product innovations, see the table Building Products for Consumer Needs below.

Building Products for Consumer Needs

The five basic product-design components (see page 3) can be used to generate differentiated products for different customer segments. In this example, we segment customers by basic buying strategy (see page 5), but the approach is designed to be used with detailed, research-driven, consumer insights

Key Components of Consumer-Oriented Product Design	Consumer Types by Basic Strategy		
	Health Value Manager	Price Shopper	Partner for Life
Benefits	• Benefits focused on health needs • Mostly generic formulary and use of mail order • Integrated incentives creating the opportunity for pricing buy-downs • Point system for multi-year rewards or renewals	• Benefits focused on health needs • Mostly generic formulary and use of mail order • Managed buy-downs through deductibles	• Benefit bundle with core health, ancillaries, life, STD/LTD, long-term care, etc. with potential link to asset accumulation • Integrated product partnerships with brand leaders
Provider Network Model	• Integrated local market health system or ACO as primary network • Series of designated centers of excellence for cardiology, surgery, oncology, etc.	• Integrated local market health system or ACO as primary network • Series of designated centers of excellence for cardiology, surgery, oncology, etc.	• Health risk assessment to help the consumer understand his or her health status • Personal health record with ongoing updates • Health improvement recommendations
Medical Homes	• Primary-care medical home for healthy and at-risk consumers • Chronic care medical home for consumers with chronic diseases • Medical home manages the patient and coordinates the care	• Primary-care medical home for healthy and at-risk consumers • Chronic care medical home for consumers with chronic diseases • Medical home manages the patient and coordinates the care	• Available if the consumer has interest
Health Engagement Models	• Health risk assessment • Health improvement plan • Specific goals and rewards for chronic disease management	• Complete health risk assessment to participate in medical home	• Available if the consumer has interest
Service Support	• Self-service model with easy interaction with the medical home • Transparent reporting on integrated incentives and health improvement programs	• Self-service model with easy interaction with the medical home	• High-touch advisory model on bundled products, health issues, and long-term planning
Consumer Value Proposition	• 10%-15% price advantage with lower renewal price and rewards for health improvement	• 10%-15% in-year price advantage	• Integrated one-stop shop considering the risk and economic aspects across benefits

Getting Started

Now is the perfect time for health plan leadership teams to develop their consumer business strategies and to start down the road to implementation: considering their design options and estimating how those choices will influence membership, revenue, short-term risk exposure, and longer-term consumer market success. We believe Oliver Wyman's "Four P's Framework" will provide a useful guide for developing a robust, competitive approach to the consumer market.

> ***Prediction:*** *Understand consumer needs and segment the consumer market into like-buying groups.*
>
> ***Product:*** *Develop an innovative consumer-driven product model that permits consumers to buy the healthcare most valuable to them.*
>
> ***Profit model:*** *Carefully align organizational competencies and pricing strategies to consumer segments and products to create competitive advantage and meet profit expectations. Reflect the value of the new network models, the medical home, health engagement programs, and services models in the pricing model.*
>
> ***Positioning:*** *Set a consumer positioning strategy that is true to the product model and resonates with targeted consumer segments—build consumer loyalty over time.*

In the next few years companies will experiment, make some mistakes, and ultimately learn how to become thriving consumer businesses. For successful companies, innovative and compelling products will be at the heart of the effort. Anything less—for example, the appealing but erroneous strategy of simply refining existing employer-based products—will be inadequate to meet consumer needs and win customer loyalty. The new consumer-driven marketplace, with its potential 100 million members, offers exceptional opportunities. Oliver Wyman believes it merits and will reward an appropriate level of investment, effort, and creativity.

About Oliver Wyman

With more than 2,900 professionals in over 40 cities around the globe, Oliver Wyman is an international management consulting firm that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, organizational transformation, and leadership development. The firm helps clients optimize their businesses, improve their operations and risk profile, and accelerate their organizational performance to seize the most attractive opportunities. Oliver Wyman is part of Marsh & McLennan Companies [NYSE: MMC].

Oliver Wyman's Health & Life Science's practice serves clients in the pharmaceutical, biotechnology, medical devices, provider, and payer sectors with strategic, operational, and organizational advice. Deep healthcare knowledge and capabilities allow the practice to deliver fact-based solutions.

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