

Pricing Medical Technology Products

Interview with Tim Irish

Senior Vice President and Chief Marketing & Strategy Officer
Philips Medical Systems

Interviewer: Christian Renaudin, TMTG

CR: Specifically, there are many methods for pricing: cost plus (engineering cost defined the price), competitive benchmarking (competitive prices define the price), value-based (price is based upon the perceived value of the product), EVA based (defined by the economic yield of the product), bundling or de-bundling with service or non-core offering like training. It seems that "cost plus" pricing is not adequate anymore and value-based pricing may prevail. Do you agree?

TI: You are right. For imaging equipment at least, we are in a big transition. We used to be engineering driven relying on cost-plus pricing. Now our pricing approach is undergoing a transition: today, we don't distinguish the pricing question from the segmentation question.

For example, a 16 slice CT launched at an initial price based upon our perceived level of innovation and technological excellence compared to our competitors and the likely competitive response to our price. Now, we try to be market driven and lump specific customers into one bucket in order to evaluate the market's price point. Then we evaluate whether engineering can meet the market requirements and whether necessary technological developments are feasible.

CR: Compared to other industries, how would you assess the level of sophistication of equipment pricing?

TI: At this stage, our customers are ahead of us: they know how to segment, to market and to price their services. We are not world class in healthcare market pricing. We are in the midst of a big and painful transition. We have to overcome organizational and capability challenges to be able to execute well.

We must pay particular attention to the macroeconomics as well as local market factors. Especially in the US, we should not assume that we will sell a volume of X systems at a price of Y without taking a close look at the customers' needs first.

High-tech and medtech equipment is more healthcare economics driven, excluding most medical imaging equipment. We need to take into account the total value of the procedure and how our technology plays an enabling role. The package, which includes hardware, software, and staffing components, has to be assessed in order to create the whole economic equation.

Overall, I think our industry lags behind most others in developing pricing strategies. Our customers tend to change at a much more rapid pace than we do. In order to be competitive, we need to stay innovative in the way we target our customers.

CR: Will the industry evolve beyond competitive benchmarking for price then?

TI: We are conceptually beyond that point. OEMs (GE, Siemens, and Philips) are creating different solutions that have clients comparing fewer offerings.

CR: Do you see a challenge with your sales channel (for example, trying to sell everything to everybody)?

TI: Yes, this is part of the problem. Currently, Philips is creating a cardiology portfolio that offers packages aligned to specific cardiology segments. The danger is that some clients could seek to procure the "same" technology outside their established channel for a better price. The ultimate challenge for OEMs is to be flexible and address this new challenge of cross-segment competition and potential confusion in product positioning.

CR: Which methods do you recommend for the pricing of a medical technology product?

TI: We have to be pragmatic. It starts with the degree that your own data accurately depicts internal pricing practice. It is important that an OEM knows what it charges each type of client across the entire market. With that said, you then need to look at your market segmentation, your value proposition and the differentiators you created that would justify a premium price.

I believe in good qualitative and semi-quantitative research first to get a sense of price. Then, go more quantitative as needed. It should be noted that nothing replaces marketing's basic questions: what does each segment need? What is the relevant competitive value proposition and price? What is the demand likely to be at a specific price point? All of these questions help shape the right price for each segment. This is extremely complex in our business since we have to integrate external factors, like regulatory approval. In this marketplace, we still have two types of organizations: those that are geared towards marketing and those that are financially driven.

CR: Have pricing simulators impacted the way Philips prices medical technology?

TI: Pricing simulators are excellent and important tools. However, they provide only one perspective. We need to have a healthy debate about pricing choices that rely on predictive tools along with qualitative feedback from clients and sales channels.

CR: Do you believe in having a global price for a product in all markets (like Mercedes or Apple do)?

TI: In healthcare, one price is an appealing but an elusive goal. Healthcare is quite political and nationalistic. In addition, we have different stakeholders; patients, providers, and payers. - a unique combination. The "one price – one product" approach will eventually become dominant, but it may take several decades.

CR: In many cases, the medical device sales person/manager can reduce price by 15% or more. Is this seemingly arbitrary tactic sustainable?

TI: List prices have not been sustainable, and as a result, they are becoming irrelevant. We are moving away as much as we can from this discount practice. At Philips, sales people have less discretion than our competitors for granting discounts. If you segment your customers properly, you can reduce the need for the ad hoc pricing changes. You can't entirely get rid of discount practices, but you can provide a good structure or framework. In short, sales channel and segment alignment is crucial - the combination will greatly reduce the need for discount practices.

CR: What is the future: increased price elasticity or reimbursement driven pricing?

TI: This is a difficult question. I would probably say both. In some ways, I see more elasticity in price. Depending on the customer segment, if the packaging practice takes off, we will see different pricing levels depending on the mix of hardware – software – biology (contrast agents).

OEMs must provide true healthcare information (i.e. the diagnostic answer) to their clients by offering a complete package aligned to their needs. In that sense, I see more elasticity when this sort of packaging practice is established. However, I also see reimbursement having an impact on price. At this point, it is difficult to predict the effect on price. The reality is that healthcare is ripe for change, but it is slow. In my opinion, the long-term trend is more towards price elasticity.

CR: How about internationally, do you see one price for all countries?

TI: I think that differences will increase between countries. We will have to sell different imaging systems per country reflecting the needs of the customer segments. There will be universal segments such as public vs. private. Each segment will feature specific needs to address. For example, for specific packages including equipment/service and contrast agents, there will be one unique price per package per segment. Bundling imaging solutions in this way makes comparisons of the component parts very difficult.

Underserved or poor regions cannot afford high-end solutions, so we cannot offer the same solutions to both poor and rich regions. For example, ultrasound handheld systems (laptop like) may be valid products in emerging markets, whereas in western markets this product would be viewed quite differently.

CR: Do you see a risk of cannibalization internationally with "rich countries" seeking more affordable solutions?

TI: There is always that risk. That is why it comes down to a package approach.

CR: Is the price of technology where it is supposed to be? Do you see some pricing erosion?

TI: The evidence suggests that innovation is declining. We have been forced to absorb the reduced "reward" for product innovation. One approach we have used to maintaining margins was to outsource manufacturing to low cost countries. Overall, I am not sure how we will be able to address the next wave of price erosion and commoditization.

I think we need to be more forthcoming in demonstrating the financial benefits of equipment. We need to eliminate this win/loss situation where the client keeps asking for discounts. This can be accomplished by creating more open partnerships with our customers.

CR: Customers perceive OEMs as abusing them in terms of product and service pricing. What could be a likely response?

TI: Again, transparency in our practice and working openly with our clients and having a mutual understanding is critical.

CR: How do you define the imaging package?

TI: Hardware on its own has reached its limits. The same is true for software or biologics as separate offerings. The TRUE product value is the combination of the above which together create an overall information value to the client. Future success will depend on who can provide the information that will best address the most critical clinical issues. Obviously, in this new environment, the boundaries between the practice of medicine and the role of OEM partner for medical technology will be tested.



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