

# The external environment - Leading Change: A Conversation with Ron Williams

Case duration (Min): **45-60**

Strategic Management (SM)

**The external environment****The internal environment****Worldwide****Case summary:**

This case may be used to explore several strategic management topics (see other case studies using this film).

Tutors must decide whether or not they have time to show the whole film or part of it (three options are provided).

Considers the EXTERNAL MACRO ENVIRONMENT and the INDUSTRY (MICRO) ENVIRONMENT for the health insurance industry. Enables students to practice PESTLE, Five Forces and SWOT analysis.

**Learning objectives:**

Understand the significance and the influence of the external (macro and micro) business environment for the organization.

Critically evaluate and apply a range of tools for analysing the internal and external environment.

**Case problem:**

Why do and how can organizations analyse their environments ?

Accident &amp; Health Insurance

**Company**

Aetna, Inc

[Aetna.com](http://Aetna.com)

Founded in 1853, Aetna, Inc. is an American diversified health insurance company, providing a range of traditional and consumer-directed health care insurance products and related services, including medical, pharmaceutical, dental, behavioural health, group life, long-term care, and disability plans, and medical management capabilities. With revenues of \$30.950 billion (2008) and a workforce totalling 35,258 (2008), Aetna is a member of the Fortune 100.

Aetna moved up on the Fortune 500 list in 2009. The company's strong gains in revenues in 2008 were largely the result of Aetna's integration and segmentation strategies, which led to strong membership gains.

The Aetna Mission:

Aetna is dedicated to helping people achieve health and financial security by providing easy access to safe, cost-effective, high-quality health care and protecting their finances against health-related risks. Building on a 156-year heritage, Aetna will be a leader in cooperating with doctors and hospitals, employers, patients, public officials and others to build a stronger, more effective health care system.

Vision :

To earn the distinction, financially and by reputation, of being the preferred benefits company in all aspects of our business. We strive to be the industry leader by including the best ideas and perspectives available. This in turn enables Aetna to develop the most relevant solutions for each of our markets.

Strategy :

Aetna will be the industry leader in the diverse marketplace. We will deliver best-in-class service to our customers because we want them to be comfortable when doing business with us. To achieve this mission we will:

Create innovative and tailored product and service solutions that will meet the unique needs of our customers.

Develop a diverse supplier base, reflecting our multicultural environment that supports innovative ways to deliver best-in-class services to them.

Build a workforce that fully understands the diverse communities where we do business.

Foster a culture of inclusion that grows a diverse talent pool and recognizes and rewards the contributions of every employee whilst allowing employees to do their best work.

Pre class activities...

- 1 Research Aetna, Inc and the (US) Health insurance industry prior to class 45-60

First, if you are taking a taught management course then consult with your tutor and ensure that the case has not been scheduled into a teaching class or tutorial. If it has not:

1. Play/ read the media associated with the case. You may need to access the Internet and enter a URL to locate any video clips.
2. Attempt the Case study questions.

Consider attempting the case study as a group exercise; you could form a study group with fellow students.

3. Check the suggested answers - remember these are suggestions only and there are often many possible answers.

Discuss questions and answers with other students.

4. If you feel your answer(s) were weak then consider reading the relevant suggested readings again (also see the case study suggested references).

Title/  
Media type

URL/ Media description

Leading Change: A Conversation with  
Ron Williams.

<http://mitworld.mit.edu/video/614>

**Film**

Williams' case study begins in 2001, when he arrived to find a corporation (Aetna) in need of change -- having lost \$280 million in the past year. He diagnosed key areas of failure and opportunity in Aetna's vast enterprise: orchestrating medical, dental and other health and insurance benefits in a network of 843 thousand health care professionals with 37 million members. Williams shaped a path to recovery, focusing on a better understanding of Aetna's current customers, from small employers to the largest corporations, and the best way of expanding into new markets such as retailers, banks and law firms. To do this, Aetna needed to build products and services suited for those groups, and Williams' strategy involved developing integrated information systems for both employers and consumers, to ensure cost-effective and high quality health care delivery.

Williams repeatedly made the case for this new strategy directly with Aetna's staff. He pressed the issue of values: integrity, employee engagement, excellent service and high quality healthcare, and instigated employee surveys and biannual performance reviews. Employees were invited to answer whether they believed their supervisors held true to Aetna's values and whether they were proud to be working with the company. Williams has noted a marked improvement in responses over just a few years. External benchmarks reflect positive growth as well: Aetna has reached the number one spot as Fortune Magazine's most admired health care company, after occupying the bottom position. Williams invested a great deal in technology which he believes will "shape the future of health care." He describes a Care Engine, containing an individual member's personal health record and up-to-the-minute journal information and health guidelines that are "converted into computer algorithms." This system can detect and fill gaps in care for patients -- conditions that go undetected, tests that should be administered, medicine that should not be prescribed. Williams has also given consumers the ability to find and compare the costs of tests and doctor visits. He believes we can check the trillions of dollars in health care spending through smart technology. For him, health care reform means we "get and keep everyone covered; maintain the employer-based system... reorient the system toward prevention, value, and quality of care; and use market incentives to improve coverage, drive down costs and make the system more consumer-oriented."

**NOTES:**

## Case study questions...

Action	Pre/During/After class
<b>1 BUSINESS ENVIRONMENT:</b> What is the business environment and why do organizations analyse it?	During
<b>2 ANALYSING THE ENVIRONMENT:</b> There are many ways to analyse and assess the environment. Environmental analysis is the process of assessing and interpreting the information gathered through environmental scanning (continuously monitoring the environment). List and describe common approaches to environmental analysis – what tools are typically used to analyse the Macro environment, Micro environment and the internal environment?	During
<b>3 INDUSTRY: HEALTH CARE: INSURANCE &amp; MANAGED CARE - HEALTH INSURANCE INDUSTRY ANALYSIS PEST ANALYSIS :</b> Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of the Health Insurance Industry using PEST Analysis (Analyses the US Healthcare Industry).	During
<b>4 AN EVALUATION OF THE HEALTH INSURANCE INDUSTRY USING MICHAEL PORTER'S FRAMEWORK:</b> Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of the health Insurance Industry using Michael Porter's Framework Analysis (Analyses the US Healthcare Industry).	During
<b>5 AETNA SWOT ANALYSIS:</b> Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of Aetna using SWOT Analysis.	During

## MACRO-ENVIRONMENT

the wider environment of social, legal, economic, political and technological influences in which the organization is situated

## MICRO-ENVIRONMENT

the immediate environment including customers, competitors, suppliers and distributors in which the organization is situated

## ENVIRONMENT

issues, trends, events and other factors outside the boundaries of an organization but which can influence internal decisions and behaviours.

## ENVIRONMENTAL ANALYSIS

The process of assessing and interpreting the information gathered through environmental scanning

## ENVIRONMENTAL COMPLEXITY

Concerns the range of external factors - customers, suppliers, regulatory agencies, competitors, - relevant to the activities of the organization; the more factors, the higher the complexity.

## ENVIRONMENTAL DETERMINISM

a perspective which claims that internal organizational responses are wholly or mainly shaped, influenced or determined by external environmental factors.

## ENVIRONMENTAL DYNAMISM

the pace of change in relevant factors external to the organization; the greater the pace of change, the more dynamic the environment (see environmental uncertainty).

## Question/ Answer

### 1 BUSINESS ENVIRONMENT:

What is the business environment and why do organizations analyse it?

The business environment is divided into the external and internal environment. The internal environment consists of all resources and capabilities found within the organization which influence the organization's ability to act (to create outputs). The analysis of the business environment allows the organization and its employees to understand the context within which they operate and thus strategy is developed and implemented. It is important to note, however, that environments are not static but constantly changing. Understanding the global business environment and its economic, social and political influences is crucial to success in today's international business world.

One of the first challenges is to recognise the enormity of factors in the business environment and therefore decompose it into manageable parts. Environmental Variables are factors affecting the organization which are beyond the direct or positive control of the organization. The external environment may be divided into layers: The Macro-environment is the wider environment of social, legal, economic, political and technological influences (forces). The macro environment contains the more general factors likely to affect organizations in a similar manner, whereas, at the industry level, the factors are of more specific concern to a specific set of organizations. The Micro-environment is the immediate (industry) environment, including customers, competitors, suppliers and distributors. One of the main factors affecting most organizations is the degree of competition faced. Greater influence is likely to come from the actions of competitors and the behaviour of customers or prospects. Markets change rapidly through the entrance of new competitors, technologies, legislation and evolving customer needs. Aside from considering the macro and industry (micro) external business environment, the organization must also analyse the internal environment; resources and capabilities.

### 2 ANALYSING THE ENVIRONMENT:

There are many ways to analyse and assess the environment. Environmental analysis is the process of assessing and interpreting the information gathered through environmental scanning (continuously monitoring the environment). List and describe common approaches to environmental analysis – what tools are typically used to analyse the Macro environment, Micro environment and the internal environment?

Making sense of the macro environment poses a significant challenge. However, there are diagnostic frameworks which help break it down into more manageable components (environmental variables) that can be investigated. PESTEL (see also PEST, SLEPT, STEP & PESTLE) analysis is a common technique for analysing the general external environment of an organisation in terms of the political, economic, socio-cultural, technological, environmental and legal aspects. Whilst a PESTLE analysis would help make sense of the macro business environment, it would not provide the detailed understanding needed to compete in the industry. Consequently, tools such as the five forces framework and industry lifecycle are used to enable a more detailed understanding of the business (micro) environment. The first stage of industry analysis is to identify the key elements of the industry's structure: the suppliers, the competitors and the customers and their relative bargaining power. In order to predict the future profitability of an industry, we must consider levels of competition and identify the trends that are changing the industry's structure. We must then consider how these structural changes will affect the five forces of competition. The actions of competitors will often be amongst the strongest influences on the organization. Porter's five forces framework can help in identifying the sources of competition in an industry. An organization must confront (1) rivalry of competitors within its industry, (2) threat of new entrants, (3) threat of substitutes, (4) the bargaining power of customers, and (5) the bargaining power of suppliers - together these determine competition in an industry or market. The Competitive forces model is used to describe the interaction of external influences, specifically threats and opportunities which affect an organization's strategy and ability to compete. Aforementioned concepts and frameworks help organizations better understand their environments as sources of opportunity and threat. The organisation's strengths and weaknesses, opportunities and threats, (SWOT) are typically analysed during the strategy formulation process. SWOT alongside PEST/PESTLE can be used as a basis for the analysis of business and environmental factors. A SWOT analysis summarises the key issues from the business environment and the strategic capability of an organisation both of which are most likely to impact upon strategy development. It involves specifying the objective of the business venture or project and identifying the internal and external factors which are favourable and unfavourable to achieving that objective. The internal factors may be viewed as strengths or weaknesses, depending upon their impact upon organizational objectives.

## **ENVIRONMENTAL FACTORS**

Factors external to the organization that influence the adoption and design of information systems.

## **ENVIRONMENTAL SCANNING**

a term for a number of techniques for identifying and predicting the potential impact of external trends and developments on the internal functioning of an organization.

## **ENVIRONMENTAL UNCERTAINTY**

the degree of unpredictable turbulence and change in the external political, economic, social, technological, legislative and ecological context in which an organization operates; the more the dimensions of the external context are interrelated, the higher the environmental uncertainty (see environmental complexity and environmental dynamism).

## **SWOT ANALYSIS**

The study of Strengths, Weaknesses, Opportunities and Threats facing an organisation that may provide a basis for decision-making and problemsolving.

## **PESTEL ANALYSIS**

A technique for analysing the general external environment of an organisation in terms of the political, economic, socio-cultural, technological, environmental and legal aspects.

## **FIVE FORCES FRAMEWORK**

a model that describes the interaction of external influences (forces) within an industry that present threats and opportunities for an organization

## **3 Industry: Health Care: Insurance & Managed Care - Health insurance industry analysis PEST Analysis :**

Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of the Health Insurance Industry using PEST Analysis (Analyses the US Healthcare Industry).

**POLITICAL FACTORS:** Changes in politics, regulations for improved Senior Health, prescription drug coverage for Medicare, lawsuits' impact on Medicine, national Health Care Strategy.

**ECONOMIC FACTORS:** recession, per capita expenditure, unemployment.

**SOCIAL FACTORS:** People are living longer, senior population, rising obesity, more knowledgeable, reliance on the Internet/ access to medical information (consumers more aware).

**TECHNOLOGICAL FACTORS:** Enterprise systems, integration software to provide unified view, decision support, knowledge management, mobile communications, Internet, E-Prescriptions, Radio Frequency Identification (RFID), broadband.

## PORTER AND MILLAR'S FIVE FORCES MODEL.

Porter and Millar's five forces model is for analysing the different competitive forces which impact on an organisation. The five forces are: rivalry between existing competitors, threat of new entrants, threat of substitutes, the power of buyers and the power of suppliers.

### 4 An Evaluation of the Health Insurance Industry using Michael Porter's Framework:

Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of the health Insurance Industry using Michael Porter's Framework Analysis (Analyses the US Healthcare Industry).

Health insurance is insurance that pays for medical expenses. It may be provided through a government-sponsored social insurance program, or from private insurance companies. It may be purchased on a group basis (e.g., by a company to cover its employees) or purchased by individual consumers. In each case, the covered groups or individuals pay premiums or taxes to help protect themselves from high or unexpected healthcare expenses. Similar benefits paying for medical expenses may also be provided through social welfare programs funded by the government. By estimating the overall risk of healthcare expenses, a routine finance structure (such as a monthly premium or annual tax) can be developed, ensuring that money is available to pay for the healthcare benefits specified in the insurance agreement. The benefit is administered by a central organization such as a government agency, private business, or not-for-profit entity. Their primary aim ought to be to buy cost-effective, efficiently-delivered care on behalf of their clients.

**FACTORS AFFECTING INSURANCE PRICES** - the drivers of rising health care costs in the U.S. include increased consumption created by increased consumer demand, new treatments, and more intensive diagnostic testing. People in developed countries are living longer. The population of those countries is aging, and a larger group of senior citizens requires more intensive medical care than a young healthier population. Advances in medicine and medical technology can also increase the cost of medical treatment. Lifestyle-related factors can increase utilization and therefore insurance prices, such as: increases in obesity caused by insufficient exercise and unhealthy food choices; excessive alcohol use, smoking, and use of street drugs.

In the US, According to the United States Census Bureau, approximately 84% of Americans have health insurance; some 60% obtain it through an employer, while about 9% purchase it directly. Various government agencies provide coverage to about 27% of Americans.

Porters Five Forces of Competition framework views the profitability of an industry as determined by the five forces of competitive pressure.

#### Competitive Rivalry (High)

The industry is a growing one, there are many competitors and Industry competition is high. Diversity among competitors tends to be low because health insurance companies are heavily regulated in terms of structure and the type of products they can or are required to offer.

Competitors: UnitedHealth Group, Wellpoint, Aetna, Cigna, Humana, Health Net, Coventry Health Care, Amerigroup, WellCare Health Plans, Medical Mutual of Ohio

#### Threat of Entry (Low)

Entry into the health insurance industry is difficult due to the high economies of scale, high capital requirements, and high government and legal barriers. Economies of scale are needed to create a collection and claims payment network large enough to provide a selection of providers for patients and also allow the insurance company to have a wide geographic coverage. Health insurance companies need to have adequate clients covered so that they have revenue from healthy clients to cover the costs of taking care of sick clients /patients and a profit margin. There are also large capital requirement because health insurance companies are required by law to have a certain amount of reserves available to pay claims at all times. Government and legal barriers not only determine the financing the health insurance companies, they also determine who can operate a health insurance company through licensing.

#### Supplier Power (Low)

Health insurance companies have bargaining power for several reasons: suppliers to the health insurance industry include hospitals and medical companies. Most suppliers have low price sensitivity due to intense competition to get on a health insurance companies provider list. Health insurance companies provide a service that is vital for a patient to be able to access a supplier's service or product. The size of the health insurance company relative to their suppliers tends to be large; consequently health insurance companies purchase health care from suppliers at a much lower cost than individual patients.

#### Buyer Power (Low)

Health care is important to buyers and costs form a large portion of a buyers total cost, especially employers; despite this, buyers (individuals, employers, and linked groups of people) have low bargaining power due to their relative small size compared with health insurance companies.

Buyer power is low when products from health insurance companies are not well differentiated. What about switching costs?

#### Threat of Substitutes (Low)

There are few substitutes for health insurance and buyers either have health insurance to cover their medical expenses or pay for health care costs themselves (or do neither, putting themselves at risk); the high price of medical care makes self-pay an unappealing alternative.

## 5 Aetna SWOT analysis:

Drawing upon information provided in the case video and your wider research and knowledge, conduct an evaluation of Aetna using SWOT Analysis.

Students may conduct an analysis for the company in 2002, 2006 or 2008/9:

2009:

**Strengths:**

**Workforce:** strong management team, motivated and engaged workforce, strong culture, values fit, Aetna way, employee engagement.

**Comprehensive product portfolio and extensive network increasing customer base:** Aetna is a single-source provider of a full range of health care, individual, and group insurance plans and programs. This makes Aetna a one-stop shop for health care and insurance plans for its clients. Extensive national network leads to better quality of customer service, since the company's customers do not have to travel long distances for health care services. Aetna has been ranked by FORTUNE Magazine as the most admired company in the Health Care: Insurance and Managed Care category for FY2008. Aetna has made significant investments in health information technology capabilities. Investments in health care technology reduces cost and enhances the quality of health care.

**Weaknesses:**

Despite a boom in the pension market, the company has not been effective in tapping the existing opportunities. Aetna needs to strengthen its operations in this segment to counter competition. Overdependence on the US market - Aetna derives a significant portion of its revenues from the US. The company, as a result, is vulnerable to market conditions in the US.

**Opportunities:**

**Healthcare expenditure growing.**

National health spending will reach \$2.5 trillion in 2009 and by 2018, it is expected to reach over \$4 trillion and comprise just over one-fifth of GDP. There are 46 million uninsured Americans looking for coverage in the individual and small group markets. Over 8 million of these uninsured are children.

**New product launches likely to increase customer base and revenues:** Aetna has introduced several new products in recent years such as Personal Health Record, which provides members with online access to personal information to help them make better decisions about their health care. The company continues to develop and enhance existing products. The company is improving transparency of products and pricing. The introduction of new products and services increased the geographic operations and the customer base.

**Threats:**

Instability in financial markets decreases profitability. This could lead to deterioration in the value of financial assets held for trading and also investments in the long term care and pension products. The company may observe a decline in investment income in 2009 and beyond. Aetna primarily operates in the US. The economy is likely to record a negative growth rate in 2009. This is likely to be associated with an increase in the unemployment rate, which may lead to a reduction in membership and thus the revenues of the company.

**Cost base growing – increased use of healthcare – new treatments, poor life style, more expensive technologies, litigation, new medication.**

## Case study references

Cole, G A. and Kelly, P P. (2011) 'Management Theory and Practice', Ed. 7. Cengage EMEA.

Kelly, P P. (2009) 'International Business and Management', Cengage Learning EMEA.

Thompson, J L. and Martin, F. (2005) 'Strategic Management', Ed. 5. Cengage Learning EMEA.