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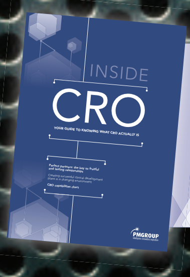

INSIDE CRO

Rohit Khanna
THE PRICE IS RIGHT

Can the medical device industry reconcile itself to the consumer trend of giving away capital assets and maximising on sales on consumables?

Over the last few years I've had the chance to work with medical device clients that have launched new products into the marketplace with, largely, disappointing results – 'disappointing' by their own internal standards which are quite high; all the products have achieved market penetration but not to the targeted sales budget levels set out for them by senior management.

As with all product launches, there are numerous issues that affect the adoption of new products: share of voice, marketing spend, regulatory approvals, market access and/or reimbursement, product efficacy or functionality and so on.

What has been interesting with these case studies is the pricing approach that has formed the overall launch strategy. Like many products on the market, most medical device manufacturers have both a capital asset as well as a consumable to sell.

Now, not all manufacturers are in this boat but for those that are, think of the razor and razor blade concept: you get the razor (handle) free but you must continue to buy the blades (which only work on the handle for which they were designed). Think also of today's cellular/smartphone markets where wireless carriers around the world will give you the capital (the smartphone) in exchange for the consumable business (the voice and data plans for which you agree to pay a certain amount of money every month over the life of the contract).

> ***"Medical device manufacturers can set the price of their product at a certain 'list' price ... "***

Unlike pharmaceutical marketers in most industrialised nations (as opposed to emerging nations), where the price to the healthcare system for a pharmaceutical molecule is heavily regulated and subject to rigorous constraints, the medical device market acts mostly, but not completely, like a consumer marketplace.

Seeing beyond the capital

Medical device manufacturers can actually set the price of their product at a certain 'list' price and apply any volume discount off the list price they choose. There is no concept of 'reference-based pricing', as we find in some pharmaceutical jurisdictions, that mutes the price of a medical device by virtue of the fact that it acts like another similar medical device.

So, if the medical device market is most like a typical consumer packaged good, then why do so many commercial leaders within the medical device industry frown upon the 'razor versus razor blade' pricing approach. In other words, why the aversion to giving away capital free with consumable revenue and profit to follow?

Parts of this answer lie in paranoia over 'brand dilution': what does it say about my product if I am giving it away free? How can a prospective customer have the confidence in my brand's functionality, particularly if it costs nothing?

Ironically, the term 'brand dilution' is the weakening of a brand through its overuse, according to www.encyclo.co.uk

The actual opposite, of course, is what is happening. The brand is being weakened as a result of a lack of use. What marketers are really referring to is brand perception and not brand dilution. Marketers are really concerned about their brand's perception in the mind of the target customer. But is this a valid concern? Does the fact that the product is being given away free have a detrimental impact on the consumer's perception of the brand?

Put aside the financial impact of giving away a free product because that is something that today's commercial leaders have to reconcile. The impact on the firm's P&L should not be a discussion point in this debate. Either you reconcile yourself to the fact that you will have to 'swallow' the cost-of-goods on your capital and hope to make it up through continued use of consumables or you don't.

The question is this: once you have reconciled the above fact, does it make a difference in adoption and utilisation if you give away your capital free? Do customers somehow feel that they are getting an inferior product (particularly if the competitor is not giving their product away free as well)?

Capital gains

In the course of endless interviews and research that I have conducted over the years, the answer is 'no'. Regional procurement agencies, buying groups or consortia and even individual doctors do not perceive a negative association with medical device manufacturers that give away a product free.

This stems from two specific trends. The first is the consumer trend of giving away capital and making up the loss in the cost-of-goods through consumable use (smartphone or razor). Clinicians are privy to today's consumer trends as much as anyone. They see Apple iPhones and Gillette razors being given away free in exchange for continued purchase of voice/data plans and razor blades. They get it.

The second trend is the move towards increased transparency in medical device procurement that is happening across the globe. Leading medical device manufacturers – the ones that always win the big contracts and keep accounts for years and years and never seem to lose market share – are openly telling both clinicians and procurement administrators that the capital is free and that the cost of capital is being made up through the use of consumables. There's nothing wrong with that. In fact, most clinicians and administrators expect as much. No one expects that capital and innovation that results in newer and better capital should be given away for nothing.

> *" ... the manufacturer who understands that free product is not a weakness will win ... "*

Much of this seems obvious doesn't it? Give away surgical equipment and medical devices and people will use them. Then why do so few companies do this? Because they are caught up in the 'negative brand perception' frame of mind. And because they want to be rewarded for their innovation. The argument that this 'new piece of equipment is better than what they have and they should pay for it' is pervasive. The reason companies continue to invest in R&D and come up with better devices and equipment is (hopefully) to develop corresponding consumables that now work with that equipment/device and result in a higher selling price for the consumables.

The suggestion here is not that you should give away the farm free. If your health authority, buying group, national government or individual doctor is willing to pay list price (or anything for that matter) for capital, then that's a great situation to be in. However, with recent trends in medical device/surgical equipment procurement being what they are, the chances are that manufacturers will have to face this situation in the near future.

The manufacturers who understand this will win. The manufacturers who understand the bigger picture, that procurers are looking for risk sharing, will emerge on top. The manufacturers that understand truly the importance of getting product into the hands of clinicians and driving positive clinical experiences with positive patient outcomes – which results in loyalty – will win.

The manufacturers who understand that a surgical/medical device requires a corresponding surgical technique that has been honed and perfected over thousands of procedures. Surgeons using this equipment and these devices are extremely reluctant to change their habits because changing habits and techniques results in new learning curves and new learning curves result in fewer procedures (until perfected and honed again) and fewer procedures means less billing for the surgeon and fewer patients treated, will win.

And, ultimately, the manufacturer who understands that free product is not a weakness and does not negatively influence brand perception because the customers that use and receive the product (clinicians and patients) are not, in most cases, the ones paying for it directly, will win.

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