

LAC/DR/NN

PNABE-405

ISN = 68845

CONSULTANT'S REPORT ON PRIVATE
SECTOR PRE-PAID HEALTH PROJECT
FOR DOMINICAN REPUBLIC

For A Pre-paid, Self-financing Health Care Project

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Date: October 10, 1985

This report is the result of work done by the consultant for AID/DR between October 1st and October 11th, 1985. It was contracted under
PIO/T No. 517-0000-3-50082

The consultant was commissioned by AID to assist in the preliminary design of its Private Sector Health Care Project (No. 517-0230) to be initiated in mid FY 1986

I wish to thank all members of Dr. Lee Hougen's staff for their assistance in helping me put together and analyze a lot of information in a very short period of time. Special thanks are due Ms. Linda Harder whose preparatory work was excellent.

Thomas C. Ramey

This report will be structured around the following outline:

- . Objectives of consultancy
- . Overview of the Dominican Republic Health care Industry
- . Definition of the health maintenance organization (HMO) concept
- . Presentation of Market study
- . Self Financing Criteria and strategy
- . Recommended steps

A. OBJECTIVES OF CONSULTANCY

The objectives of the consultancy, based on AID/DR's IQC request, were two fold:

1. identify appropriate provider and beneficiary groups to establish a private sector HMO type project (pre-paid health plan)
2. assist AID/DR in "designing an appropriate feasible health care project"

In order to give structure to these objectives, the consultant made inquiries to AID/DR staff regarding further interpretation of the stated objectives. The consensus derived from this discussion was AID's specific interest in identifying a group (s), and in designing a health care project, that would be both self financing and private sector based. Additionally, in order to respond to AID's mandate, AID/DR was also interested in a design, which would extend a self-financing, private sector based, health care project to people on the lower end of the socio-economic spectrum. With this further refinement of objectives, the following feasibility objectives for a pre-paid health project were added:

- . serve population with adequate disposable income currently not receiving private health care
- . be self financing
- . be affordable

- . improve over all health care delivery accessibility and efficiencies
- . serve urban population

The rationale behind these refined objectives are essential to ensuring that the overall goals of the proposed AID project are met. An explanation follows:

- * Serve population with adequate disposable income currently not receiving private care.

The presence of disposable income means the option of choice and ability to pay, regardless of the position of an individual or family on the socio-economic scale. The ability to pay is the fuel which feeds a self financing mechanism.

- * Be self financing.

Although this repeats what has been stated earlier, it is worth repeating. Self financing means it generates a sufficient revenue stream to cover costs as well as surplus revenues for growth in order to allow the business to thrive on its success in the market place. For AID, this means a project without recurrent costs. It also means a project which survives and thrives because of its viability in the market place.

- * Be affordable.

In order for the project to be self financing as well as serve a population not currently receiving private health care, it must be affordable. If it is not affordable by current market measurements, it should not be subsidized in anticipation of future affordability.

- * Improve overall health care delivery accessibility and efficiencies.

A by-product of this effort should be the creation or enhancement of a delivery service system (s) to offer greater health care opportunity through better delivery of health services. The achievement of this in a project which is self financing should force competitors to adapt similar measures in order to hold on to, or expand, their market share.

* Serve Urban Population

Due to the urban area being the place of concentrated population and concentrated health care services, it becomes a necessary key target of this project. The project is dependent on economies of scale and networking. Realistically this will only occur in urban areas, specifically Santo Domingo.

B. OVERVIEW OF THE HEALTH CARE INDUSTRY

The health care industry in the Dominican Republic is dominated by the public sector, primarily by the Secretary of Public Health (SESPAS). By conservative estimates, SESPAS covers 40 to 60 percent of the population. The Social Security system (IDSS) and the Armed Forces cover another 5 percent and 3-4 percent of the population, respectively. The private for-profit sector covers about 20 percent of the population (predominantly urban), and the non-profit private sector may cover another 5 percent. (Figure 1.)

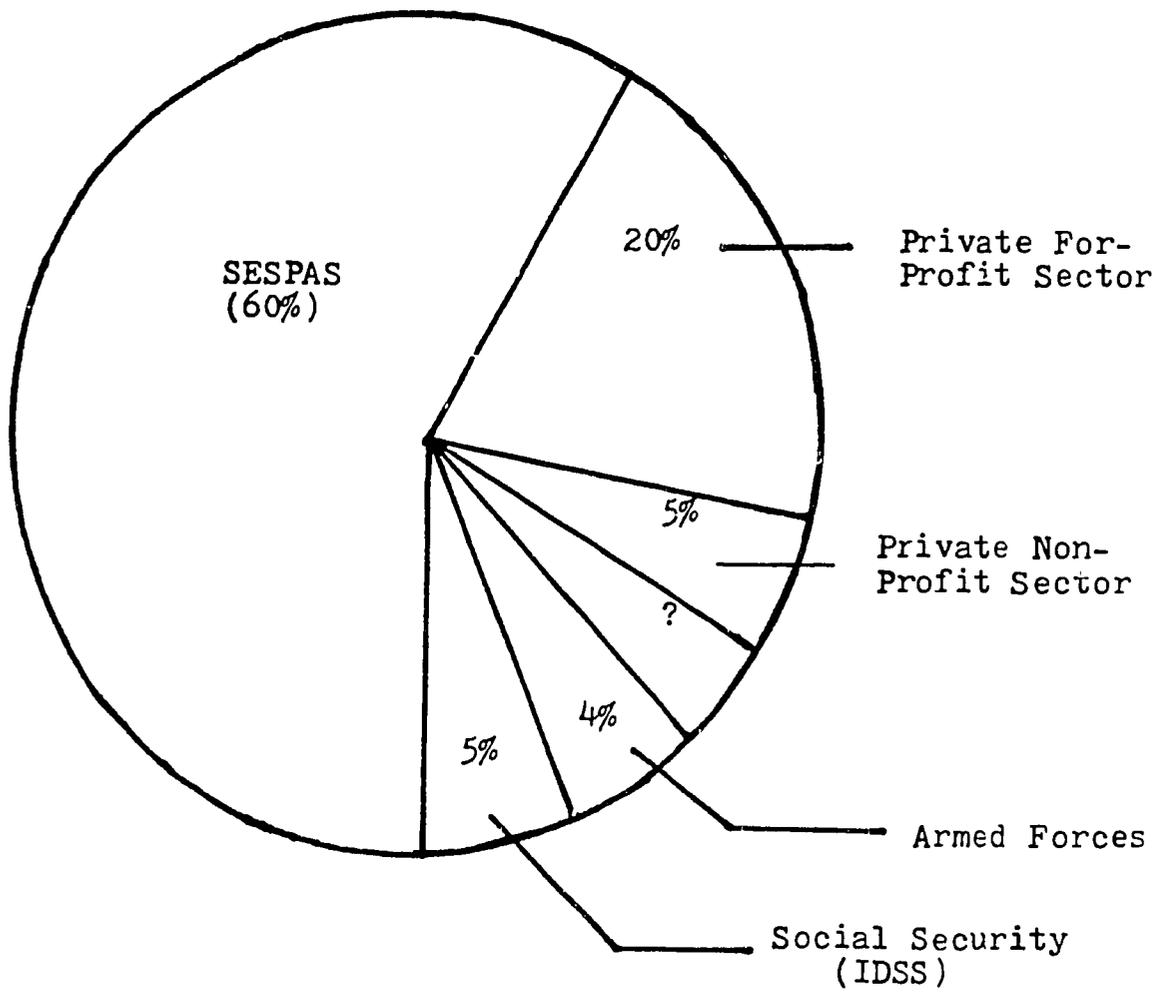
The private for-profit sector can be further sub-divided into fee-for-service clients or those who have pre-paid health coverage. Each of these segments comprises roughly 10% of the population. About half of the pre-paid population is covered by about 4 traditional, indemnity insurance companies. The other half is covered by about 15 "Iguales Medicas", or quasi-Health Maintenance Organization (HMO's). (See Figure 2.) For-profit services are primarily concentrated in Santo Domingo.

An HMO is an entity which assumes a contractual responsibility to provide or assure the delivery of health services to a voluntarily enrolled population that pays a fixed premium that is the HMO's major source of revenue. Both it and the physicians and hospitals with whom it contracts are generally at financial risk and therefore have incentives to be cost effective as well as encourage preventive rather than curative services. The HMO concept arose in the US in response to concerns about the high cost of health care.

Iguales Medicas resemble HMO's except that they provide less comprehensive services, have less developed management and control systems, and do not place their providers at financial risk. This "Iguala" concept arose in the Dominican Republic as a means of providing a "captive" market of patients for physicians, rather than as a means of controlling spiralling health care costs.

Figure 1

BREAKDOWN OF THE HEALTH CARE INDUSTRY
BY POPULATION SERVED

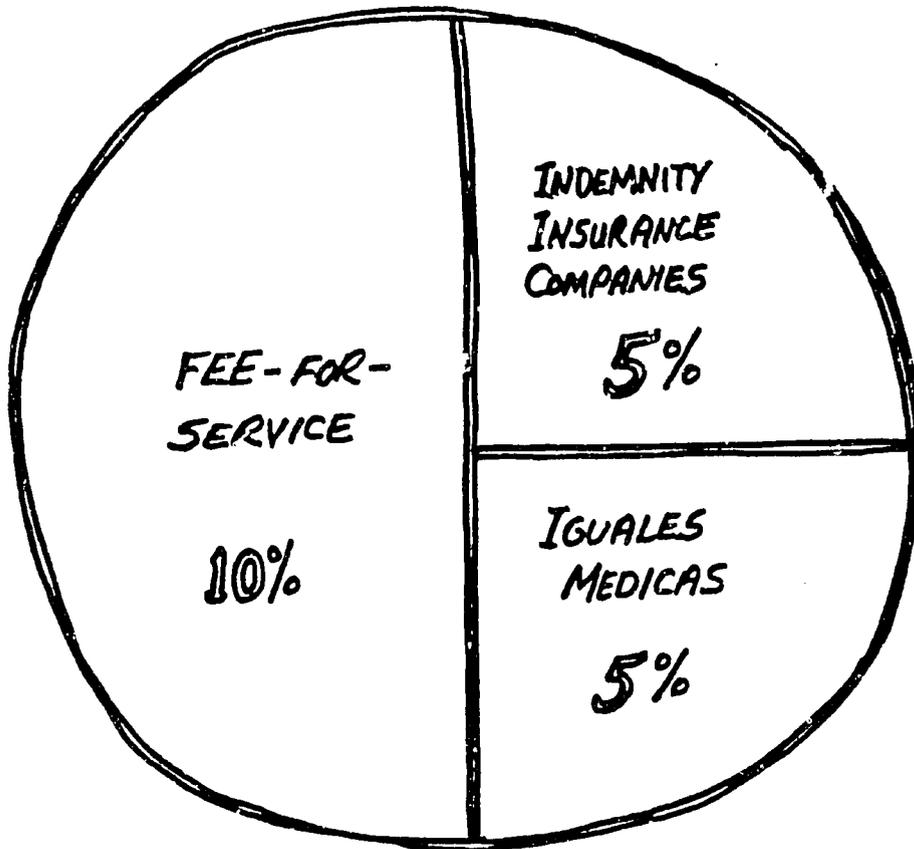


* Figures are approximate

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FIGURE 2

BREAKDOWN OF PRIVATE FOR-PROFIT
SECTOR
(20% OF TOTAL MARKET)



* FIGURES ARE APPROXIMATE

C. A MARKET SURVEY OF ALTERNATIVE PROVIDER AND BENEFICIARY GROUPS IN THE PRIVATE SECTOR

The following provider and beneficiary groups were considered potential project participants for a self-financing project:

PROVIDERS

BENEFICIARIES

- | | |
|-------------------------------------------|-----------------|
| 1) Non-Profit | 1) Individuals |
| . Catholic Church | 2) Associations |
| . Protestant Church | . Employer |
| . Private Voluntary organizations | . Coops |
| . Philanthropic organization | . Unions |
| | . Community |
| 2) For-Profit | 3) Companies |
| . Fee-for-service groups/physician groups | |
| . Traditional indemnity insurance Cos. | |
| . Iguales Medicas | |

The largest of the non-profit providers is the Catholic Church, whose parishes operate over 90 health clinics throughout the country. The Catholic Church also has a development agency, Caritas, which manages medicine distribution, agricultural, and nutrition programs. Based on size, the Catholic Church would be the ideal alternative provider to the public sector; however, its clinics are all managed individually. It also suffers from some of the elements lacking in other non-profit sector entities. In general, the private non-profit sector agencies lack:

- . Pre-payment experience
- . sufficient networks and infrastructure
- . efficient management
- . financial self-sufficiency

In the for-profit sector, fee-for-service groups also lack:

- . Pre-payment experience

- . sufficient networks and infrastructure

Traditional insurance companies, on the other hand, have pre-payment and actuarial experience, efficient management, and control systems and contract experience with companies. They lack, however:

- . Provider contract experience
- . Experience with lower income populations
- . Infrastructure
- . Provider management and cost control experience

The "Iguales Medicas" emerged from the survey as the most appropriate/feasible provider groups for an HMO-like plan for the following reasons:

- . Prepayment experience
- . Provider and contract experience
- . Healthcare network
- . Marketing experience
- . Already work with a client base which has a significant portion (40%) of low wage earners
- . Have basic management and control systems in place.

BENEFICIARIES

On the beneficiary side, individuals were regarded as poor candidates for an HMO-like plan because:

- . Tend to "self-select", (i.e.: only the already-sick will tend to sign up)
- . No "co-payer" exists
- . Premium collection too difficult
- . Expensive to market plan to individuals

Associations of employers, employees, or community members were seen as more appropriate, though still risky, candidates for a self-financing project. They were seen as risky for the following reasons:

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- . limited management discipline
- . limited capital and financial management
- . limited collection mechanisms (for premiums)
- . limited co-payment ability
- . in some cases, unstable populations

Companies which are not currently providing private health services to their employees were considered the most appropriate and least risky beneficiary population, especially given the advantages described below:

- . Employer can serve as co-payer
- . stable population
- . existence of collection mechanisms
- . employer can make participation in preventive health programs mandatory

To summarize, this study found "Igualas" to be the most appropriate provider groups and companies to be the most appropriate and least risky beneficiary groups. Associations may be viewed as potential beneficiary groups in the later project stages.

Some mechanism to improve the management and control systems of the "Igualas" and to put physicians at risk should be incorporated into the project design. The recommendations at the end of this report will address this issue.

D. SELF FINANCING CRITERIA

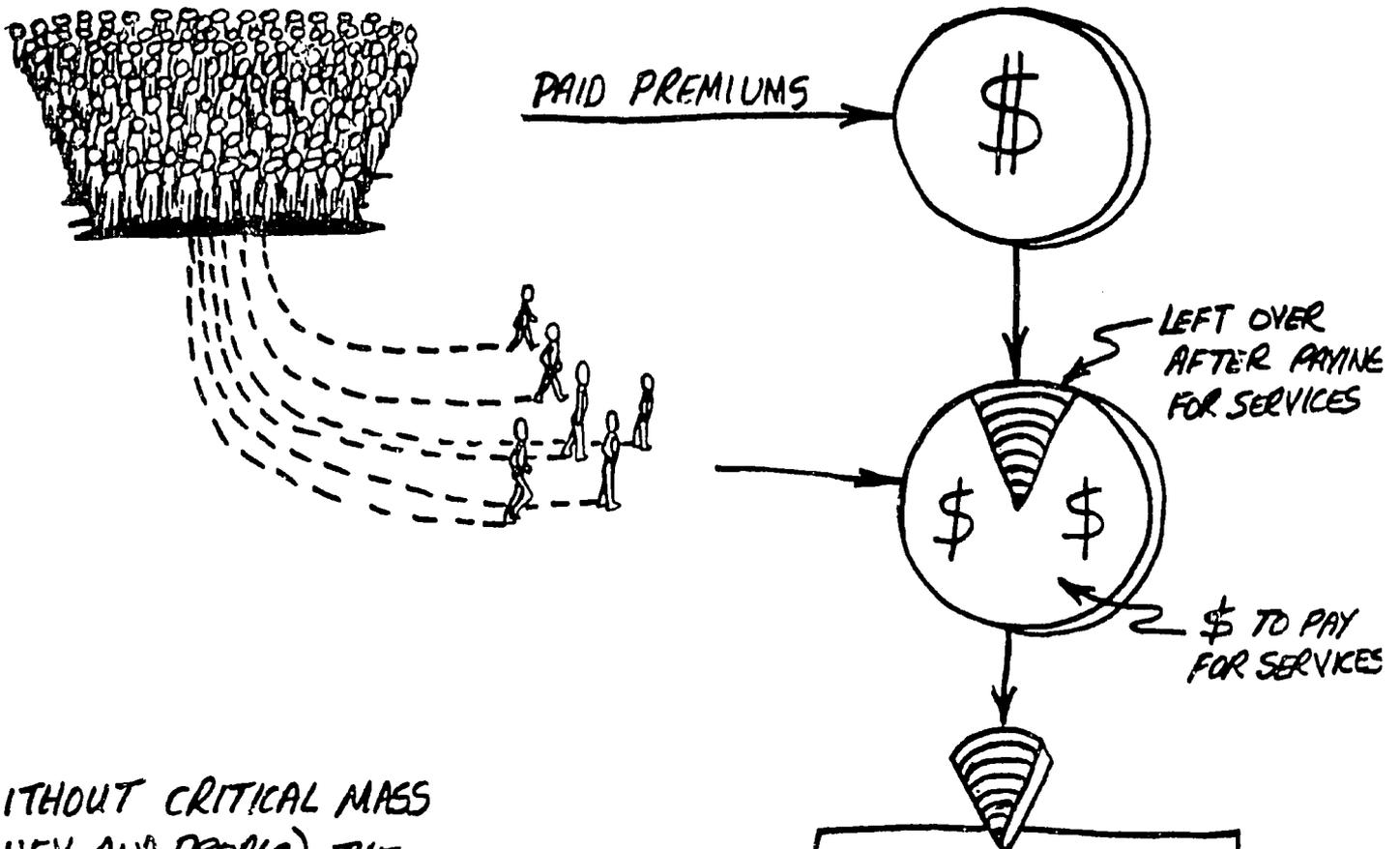
There are two criteria essential to ensuring the success of this proposed self-financing health care project:

- . critical mass concept
- . networking

The critical mass concept means attracting a sufficient quantity of pre-paid enrollees (they pay before receiving services) to allow the health care business to provide services at reduced costs due to the sheer number of enrollees and the probability that only a moderate percent of them will use the offered services at any given time. The following diagram may help to clarify the concept.

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CRITICAL MASS CONCEPT

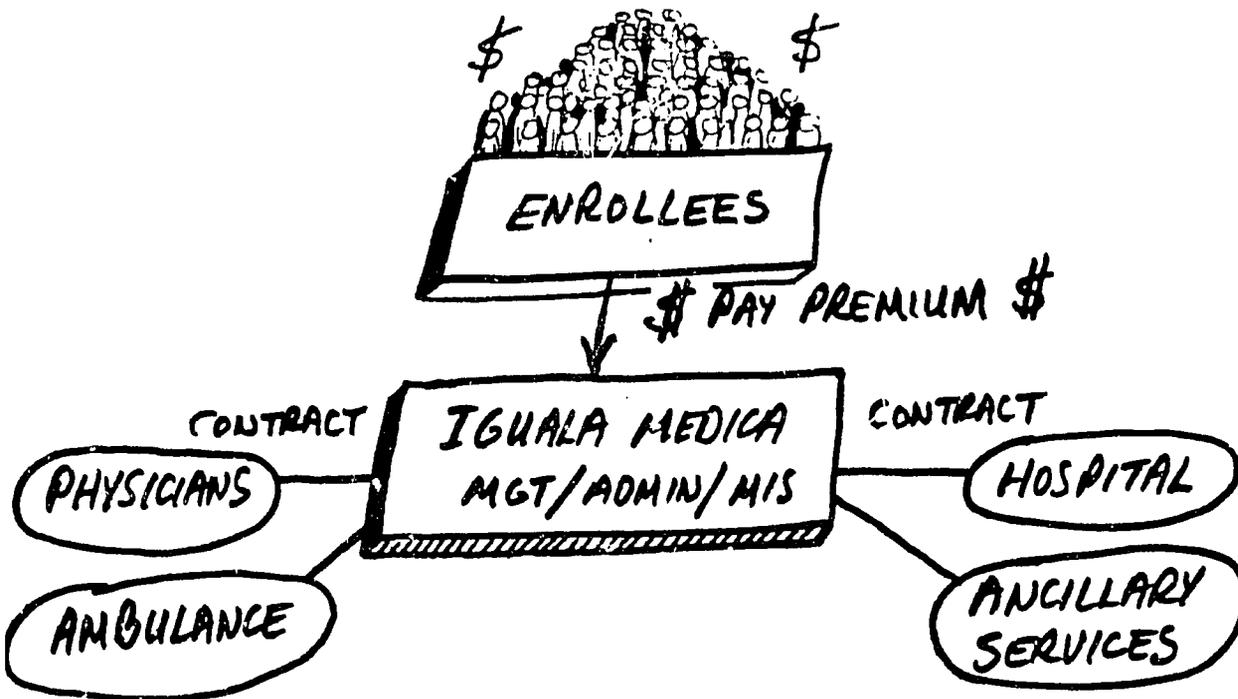


WITHOUT CRITICAL MASS
(MONEY AND PEOPLE) THE
FOLLOWING OCCURS:

- NO ECONOMIES OF SCALE
- NO FINANCIAL RISK MARGIN
- NO DEVELOPMENT CAPITAL
- NO SPREAD OF HEALTH RISK

- SERVICE DEBT
- EXPAND
- MARKETING \$
- REINSURANCE
- PROFIT/INCENTIVE POOL

Also essential is a network. Network in this regard, means a comprehensive grouping of providers such as hospitals, clinics, ancillary services, and physicians. A typical network would graphically look something like this:



In other words, the enrollee pays a monthly premium to the Iguala Medica to provide him/her with a comprehensive range of services. In order to do this, the Iguala Medica must have via contract and /or ownership, an infrastructure of physicians, clinics, hospitals, etc. to deliver services to the enrollee. Upon presentation of identification, the enrollee should receive the services stipulated by agreement through his/her selected plan.

At this point time should be taken to delineate the difference between a pre-paid service versus a fee-for-service approach, so there is no confusion between the nature and implications of the two approaches:

Pre-paid service is based on a large group of people paying for anticipated services. Only a moderate

percentage will use them. Prices are therefore discounted because not everyone uses the services.

Fee-for-service is based on demand for service when needed, paid for when delivered. It is a cost plus operation. Only when people are sick do they use the services

This clarification of approaches is important in order to assure one does not confuse the significance between the two approaches. One seeks a prepayment for anticipated services, attracting large sums of up front capital from people who are not sick; the other receives money only when the service is delivered--it is delivered when the person is sick. In the case of the former there is tremendous incentive to keep one's enrollees healthy.

The Iguala Medica, then, is a pre-paid health insurance plan with its own contracted network of physicians, clinics, hospitals and, in some cases, ancillary services. It has experience in serving minimum wage employees. It also has experience in marketing, billing, and monitoring delivery of services. The Iguala Medica provides us the basic infrastructure from which to launch an improved and expanded affordable pre-paid health plan to a larger segment of minimum wage, and under, employees.

HOW TO REACH THE UNTAPPED MARKET

To expand the urban employed population served by the Iguaias Medicas, there are four strategies:

1. add new company contracts (versus individual contracts)
2. outreach to more employees earning minimum wage and under
3. add other physicians and practices
4. provide more affordable benefit packages

COMPANY CONTRACTS. This approach to the market place offers the Iguala Medica seven advantages:

1. Marketing is less expensive when one approaches groups rather than individuals.
2. A company, being a group of insured people, distributes the actuarial risk based on the group size.
3. Enrolling as a group eliminates the risk of self selection which is not true with the

individual enrollee. In other words, if just individuals enrolled, rather than groups, it is quite likely the majority of enrolling individuals would have health problems already.

4. It is easier to provide preventive medicine services when relating to an organized environment rather than individuals.
5. Companies have people which are employeed. Being employed generally means they are more stable as a group finanically and socially.
6. Company enrollees offer the possibility of their employer co-paying for premiums.
7. Contract negotiations between the Iguala Medica and the company it is serving will be easier than having to negotiate each contract with an individual.

OUTREACH TO MORE EMPLOYEES EARNING MINIMUM WAGE AND UNDER

There are three considerations here:

1. The market study and subsequent interviews indicate this pool of people exists and that they have the capacity to pay for private health insurance. Therefore, this population is a viable market target for an Iguala Medica seeking to expand its market share.
2. People who earn much less than minimum wage have not been targeted, because the project is dependent on people being able to pay for the private health insurance they will receive.
3. It is important from a delivery of service and business perspective that this target population be stable. This usage zone is seen as being sufficiently stable. About 40% of current Iguala Medica enrollees are minimum wage earners.

OTHER PHYSICIANS AND PRACTICES. Physicians are a key ingredient in any pre-paid health care system. Adding physicians enhances the Iguala by:

1. Allowing the Iguala to contract with physicians and group practices already working in the neighborhoods where the new client base will predominantly reside fosters enrollee access. This incorporates a new percentage of physicians into the Iguala mechanism.

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2. This allows the Iguala to amplify its capacity, building on physicians and practices already strategically located.
3. Involving other physicians and practices may justify the creation of outpatient care centers in geographically appropriate areas for the projected new enrollee base. Such sites can be useful marketing and service delivery sources.

MORE AFFORDABLE BENEFIT PACKAGE In order to serve this minimum wage and under group, an affordable benefit package must be offered. It would have the following structure:

1. Offer a primary care/outpatient plan with maternity inclusion, with hospitalization and speciality care options
2. Include a strong preventive care component

All of these elements would form strategic components for expanding an Igualas enrollee base. From AID's perspective, the initiation of this project through an Iguala Medica should be able to achieve the following objectives:

- . Expand enrollee base at the level of minimum wage and under
- . Reduce costs of delivery of health care services
- . Create a higher standard of delivery capabilities
- . Expand network of facilities available to enrollees
- . Initiate market competition which will prompt other Iguala Medicas to imitate the AID project's mode of doing business and capturing market share

E. SELF-FINANCING STRATEGIES

What strategy then must AID pursue in order to make this happen? First, the existing mechanism on which this project is based is the Iguala Medica. The Iguala Medica is an existing Dominican pre-payment private sector health care delivery system, based on the critical mass concept to provide pre-paid health. The Igualas have service delivery networks already established. AID, then, has already identified a significant pre-paid mechanism already in

place, although quite rudimentary in its development. Second, by providing technical assistance and financial resources, AID can help a selected Iguala Medica:

- . improve its efficiencies and costs
- . provide a more affordable benefit package
- . expand its market share to minimum wage earners and under
- . create a model pre-paid health insurance business which will be replicated in the market place.

There is a great deal of room for improvement in the Iguala Medica structure. This circumstance exists because the Iguala has been used primarily as a marketing tool for physicians. That is, because of the excess of physicians in the Dominican Republic, physicians have had to have a vehicle for capturing and stabilizing their required market share. The use of pre-paid contracts (commitments) has been a valuable way of approaching this need.

AID is in an excellent position to use the Iguala mechanism to achieve its goal of a self financing, private sector project reaching an expanded and heretofore excluded segment of the population, while addressing the Iguala's need to be more efficient, affordable and far reaching.

There are three activities which will be required, using AID's resources, in order to accomplish these objectives:

1. Feasibility study
2. Technical assistance and start up Grants
3. Loans

1. Feasibility study--pre-paid health insurance is a very complex business. Extending its benefits to lower income people makes it even more complex. Consequently an indepth feasibility study of health care costs, current insurance programs (both pre-paid and indemnity), actuarials, actual business status of current Igualas Medicas, demographics, and the structuring of financial pro formas needs to be done. The result should be a combination feasibility study/business plan.

Estimated Cost: \$150,000 U.S.

2. Technical assistance and start-up Grants--without grants to cover the start-up costs, these monies will have to be included in loans the Iguala Medica would obtain to launch the new business effort. The cost of servicing this start-up debt would be included in the benefit package cost.

If AID wishes to reach an expanded population base, it can relieve this debt burden, (start-up cost debt) and thus contribute significantly to keeping the benefit package premium down, by granting money for start-up costs and technical assistance. This also serves as an attractive carrot to an Iguala Medica to participate, as well as to relinquish some control in order for the technical assistance providers (the U.S. company) to exert their influence.

Examples of start-up costs are installation of an M.I.S. system (hardware and software), utilization review and quality assurance manuals, negotiation of capitated contracts, marketing strategy and initial implementation, new equipment, structuring of benefit package, and organization of financial management.

Estimated cost: \$250,000-450,000 U.S.
(if equipment included).

3. Loan--As a further incentive to the Iguala to participate in achieving AID's objectives, plus ensuring the impact of the technical assistance to be provided, attractive loans (or loan) should be available to provide capital to:

- . bridge gap until break-even point is reached
- . hedge risk with new line of business
- . up grade equipment inventory

Estimated Loan: This obviously will depend on the financial proformas. The range may be from US \$500,000 to \$2 million, depending on the equipment desired.

SUMMARY OF ANALYSIS

They were four essential ingredients which guided the selection of an appropriate provider.

- . ability to achieve economies of scale (critical mass concept)
- . presence of network to provide service

- . exposure to pre-paid concept
- . ability to provide services to the minimum wage earner

The Iguala Medica scored highest on all four points.

Beneficiaries were reviewed in detail. For the following reasons, companies were identified as the best focus for reaching beneficiary populations:

- . company as a group distributes actuarial risk
- . marketing costs are less
- . easier to institutionalize preventive medicine through a company
- . more stable population
- . company will co-pay
- . ease of contract negotiations

The Iguala, with appropriate guidelines from AID (if AID is providing grant and loan money) should select which companies to market and enroll. This should be a function of the Iguala's business plan. This business plan, if AID's funds are involved, should be structured with AID's objectives in mind. However, AID, in stipulating its objectives should be as general as possible in order to give the Iguala latitude in carrying out its business.

If AID can make the support funds available as described earlier (i.e. feasibility study money, grants for start-up and loans), an Iguala, with a U.S. partner providing technical assistance, should be able to increase its enrollement by 15,000 in 3 years.

The premium structure for the minimum wage earner would be in the range of from 6 to 12 pesos per person. I have included the upward range of 12 due to increases all those interviewed said they would be making in the next four months. This also presumes a continuing inflation rate of 35%. It takes into account the probability of this project requiring 12 to 18 months from start to implementation.

The benefit package offered would be out-patient with a maternity inclusion. There would be options available. The initial package would look something like this:

OUT-PATIENT CARE

- office visits for treatment (adult and pediatrics)
- consultation and treatment by specialist
- minor surgery
- preventive services: routine eye, hearing, physical exams and immunization
- laboratory, X-ray, and diagnostic testing
- gynecological exams/pap smear
- well newborn care
- allergy-diagnosis and treatment
- family planning services
- rehabilitation therapy
- prescription medication (with co-payment)
- medications, injections, immunization, dressing, splints, casts

MATERNITY CARE

- complete hospital and doctor office obstetrical care, including:
 - . pre and post natal visits
 - . hospital services for mothers and newborn

PROVISION OF TECHNICAL ASSISTANCE

The major remaining question is how to structure the provision of appropriate "technical assistance" to the Iguala. The origin of this "technical assistance" should be from a U.S. based company with pre-paid health experience in both implementation and management. Ideally this company should not be a consulting company, rather an equity investor in pre-paid health plans. Additionally it should have international experience in pre-paid health plans.

"Technical assistance" has been put in quotes because the objective should not be strictly "technical assistance", but instead a joint venture or risk management arrangement between a U.S. company and the Dominican counterpart company. Short of either of these two arrangements, straight technical assistance might be considered. In order of priority, then, the structures would be:

1. Joint venture with equity investment
2. Risk management contract
3. Straight technical assistance

1. JOINT VENTURE

The most attractive way to involve a U.S. company and guarantee a long term commitment would be by having a U.S. company invest with a Dominican company. An attractive candidate in the D.R. to attract this type of investment from abroad would be a major insurance company such as an ALICO or Universal. The Iguales Medicas generally do not have the capital base or business acumen to give a sense of comfort and capability to a foreign investor. However, the combination of a joint venture with a U.S. investor, a major insurance company and an Iguala Medica would be ideal. The three participants would bring the following ingredients to the business:

- | | |
|----------------|------------------------|
| U.S. Company: | . prestige |
| | . technical assistance |
| | . capital |
| D.R. Ins. Co.: | . capital |
| | . sales force |
| | . actuarials |
| | . existing client base |
| Iguala Medica: | . clients |
| | . infrastructure |
| | . physicians |

The marriage of the three would be inspired by the mutual desire to expand market share, build on the others' strengths, and the favorable financial conditions AID would make accessible.

AID's role in facilitating this marriage is the key. In essence, it will provide the "carrot" to make this proposition acceptable from a risk and capital perspective to both the U.S. company as investor, the Insurance company as investor, and the Iguala Medica as provider. Each party will be encouraged to negotiate a stock relationship with the other because the financial incentives are too favorable to pass up. All parties will see these circumstances as a means for meeting their respective objectives.

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To initiate this process, though, it will be important to have the relationship between the three parties understood before the feasibility study is launched. Ideally all three should participate in the study so it can address their concerns equally. If a study were done without the participation of the U.S. company making the investment, the U.S. company would be suspect of its conclusions. As a result, it would want to do its own feasibility study before committing to this project, thus costing AID additional time and money. It is very important to have the U.S. involved from the inception of the proposed project.

IN SUMMARY

AID can help forge this marriage by:

- . funding a feasibility study to be carried out jointly by U.S. and D.R. companies, committed to invest if the project proves feasible.
- . provide grants for initial start-up, thus eliminating need for start-up debt.
- . provide low interest rate loans with generous terms, as another means of reducing risk and stimulating the project.

2. RISK MANAGEMENT CONTRACT

The second most attractive approach would be to have an Iguala Medica structure a risk management contract for three years with a U.S. pre-paid health care management company. This contract would have the U.S. management company manage, in partnership with the Iguala Board, the Iguala Medica. Risk management in this case would mean an incentive plan which would provide a bonus to the management company if certain, established benchmarks were achieved. If they were not, depending on how the agreement is reached, only costs would be covered (no fees, profits).

To do this, the C.E.O. and C.F.O. would have to be employees of the management company. The management company would be paid a fee by the Iguala Medica. The Iguala Medica would also cover the cost of the CEO and CFO. This approach would have the Iguala Medica contracting the management company. It is unlikely an insurance company would participate in this approach due to the absence of investment by the U.S. company. An insurance company would want to see a stronger financial commitment by the U.S. company since the technical assistance on which the project depends would come from the U.S. participant.

The negative side is that the commitment by the U.S. company is less. The positive side is that T.A. is made available in a comprehensive way, and the U.S. company has positive incentives to make the business work.

3. STRAIGHT TECHNICAL ASSISTANCE

This would be the provision of technical assistance by the U.S. company, funded by AID, to an Iguala Medica. This implies short term assistance to set-up the systems and strategies necessary to penetrate the identified market as well as achieve the efficiencies described throughout this report.

AID should still fund the feasibility study as well as provide start-up grant monies and attractive loans.

The major negative to this approach is the absence of a committed vested interest by a U.S. company. The positive side is T.A. would be made available, systems put in place and a comprehensive strategy developed for reaching the target population. Negotiating this arrangement is less complex.

Additionally, it would be easier to structure this type of arrangement than the capital participation and ownership of three different companies, as suggested under the joint venture.

STEPS TO IMPLEMENT

There are time frames involved which are useful to note as well as the substance of the activities within them.

SELECT AN IGUALA MEDICA

3 WEEKS

Criteria needs to be refined for selecting the Iguala which will be key to this project. As a minimum it should meet the following qualifications:

- . have a large enrollee base (in the top 10% Igualas in the D.R.)
- . have a credible (solvent and well managed) business record
- . have a comprehensive service delivery network already established
- . have experience with minimum wage employees
- . be eager to absorb and incorporate new technology

- . physicians are already accustomed to dealing with pre-paid programs
- . physicians and health facilities are accustomed to negotiating pre-determined fees for groups
- . there are pre-paid health plans with years of experience
- . current pre-paid health plans already have some minimum wage people enrolled
- . major insurance companies are contemplating pre-paid health plans a la HMOs as business objectives.

These circumstances are accompanied by another set which are also quite favorable for further developing affordable pre-paid health plans.

- . there is an excess of physicians
- . people are complaining extensively about public sector health care
- . health care costs in general are creating a problem for private sector providers
- . companies already pay for private health care policies

AID has the opportunity to attract a U.S. health company and its technology to the D.R. The U.S. company will bring its resources, both capital and technical assistance. The net result will be a substantial improvement in the way health care is delivered by the private sector in the Dominican Republic. If AID provides the "carrots" described earlier (feasibility study money, grants and loans), AID will be able to guide the provision of these self-financing health care services to a greater segment of the wage earning population on the lower end of the socio-economic scale. This project, if successfully launched will set the standard for other pre-paid health insurance businesses. Competition will cause replication of the new standard, if for no other reason than competitors will want to retain or enhance their market share.