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Inside the US stimulus program: Implications for three industries

The US government is beginning to spend vast sums to jump-start the economy. The opportunities for the private sector are huge, but so are the changes it must make to benefit from them.

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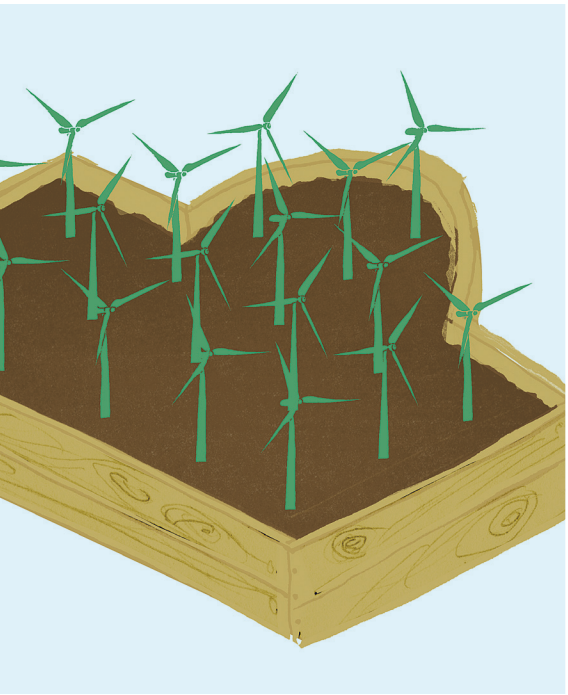
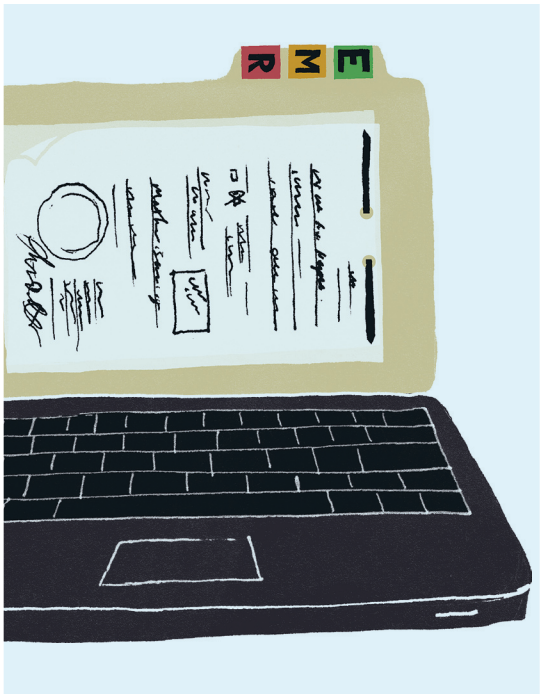




This essay introduces a package of articles that examines the US stimulus program broadly and explores its impact on three sectors in particular: health care, energy, and broadband.

The American Recovery and Reinvestment Act (ARRA) of 2009 represents the largest government intervention in the US economy since the New Deal. The total cost comes to a towering 5.4 percent of GDP—almost equal to federal expenditures on everything but military and mandated social programs during 2008. More than 70 percent of the money is to be spent by the end of fiscal year 2010.

A plan of such scale and reach comes with risks of mismanagement, perhaps even fraud, as funding flows to states and localities. But the act also portends vastly different terms of engagement between the government and the private sector. From energy to high tech to health care and beyond, major sectors of the US economy will feel the effects of policy, spending, and regulatory changes embodied in the stimulus and perhaps in a broader set of government interventions that are still under discussion.

The plans for the energy sector exemplify many aspects of the new approach (see "The US stimulus program: Investing in energy efficiency," on mckinseyquarterly.com). The Obama administration has set three sweeping goals: to create millions of clean-energy jobs over the next decade, to cut oil imports by two million barrels a day over the same period, and to slash greenhouse gas emissions by 80 percent, to levels below those of 1990, by the year 2050. The ARRA's $97 billion[1] in energy-related funding is only the first step. Separate energy and climate bills now under debate include far-reaching provisions, such as cap-and-trade polices for carbon dioxide emissions. The 2010 budget would establish a regulatory framework to recast the energy sector's fundamental economics.

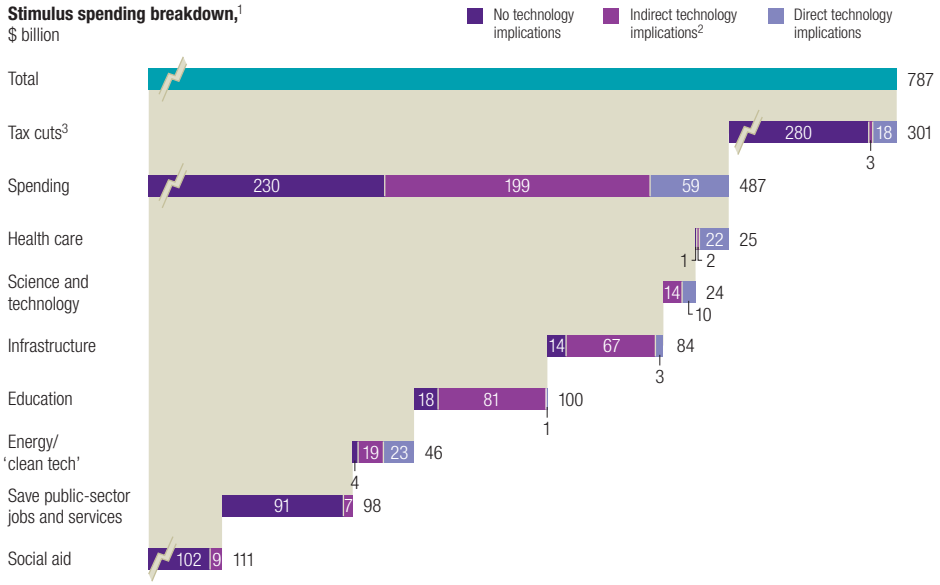
In high tech, government spending will touch nearly every subsector, with projects running the gamut from airport security installations and software for tracking student performance to systems integration work in federal agencies and optical fiber for new rural broadband networks (see "The US stimulus program: Improving broadband access," on mckinseyquarterly.com). Our analysis shows that $60 billion will be targeted directly at high tech and telecommunications. Including indirect government technology outlays, the level of expenditure rises to well over $200 billion: every major construction project funded by the ARRA will need computers, software, and IT services, for example (exhibit).

As the new reality takes shape, companies in the affected industries must rethink their strategies and organization. Some may be skeptical of deep engagement with the government, while others will leap at the opportunities offered by the stimulus. For companies that want to participate, developing the capabilities needed to flourish in this new world should become a critical priority. Some companies that haven't dealt with the government before will need to develop new skills—in contracting, for instance.

[1] Of the $97 billion, $46 billion will be spent on energy-specific projects. An additional $21 billion represents energy-related tax credits. The final $30 billion consists of broader spending initiatives with an energy component (such as funds for building renovations that include energy-efficiency investments).

Exhibit

Direct and indirect benefits for high tech



[1] Figures may not sum to totals, because of rounding.
[2] Refers to categories of expenditure that could result in technology spending. For example, spending on new bridge or road construction could generate technology-related spending on software (eg, computer-aided design) and traffic control technology.
[3] Refers to tax cuts for use of "clean technology"—ie, technology that employs renewable materials and energy sources.

Source: US Congressional Budget Office (2/13/2009); House Committee on Appropriations

The health care sector offers examples of how product development, pricing, and channel strategies could change. The government will spend $40 billion[2] to subsidize the use of electronic medical records (see "The US stimulus program: Taking medical records online," on mckinseyquarterly.com). Technology vendors will thus have a chance to serve a new market: small and midsize physicians' offices, often with fewer than five MDs each. Government spending should increase the adoption of electronic records from 5 percent of doctors now to 90 percent by 2019, according to the Congressional Budget Office. Vendors in the e-health arena (hardware, software, and IT services companies) must therefore rethink marketing strategies that target only larger companies. Many must not only learn how to offer flexible, physician-friendly products (such as software-as-a-service[3] systems) but also reorient channel strategies to accommodate a sprawling, fragmented market of 400,000 doctors' offices.

[2] We estimate that the ultimate net cost to the government is $25 billion, because the $40 billion in total spending should be offset by around $15 billion from cost savings enabled by the investment and penalties paid by nonparticipants.

[3] Internet-based systems that can be tailored to the requirements of physicians and eliminate the need for expensive specialized hardware and the associated cost of support.

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An increased government presence in many sectors will also force companies to test new organizational structures that knit together disconnected parts of the enterprise. The product-development, sales, marketing, and government affairs functions, for example, will need better models of collaboration. Already, many companies are setting up "war rooms" that assemble cross-functional teams to identify, prioritize, and capture the opportunities the stimulus spending presents. These teams, combining sales representatives with managers who have regional, product, or public-sector expertise, focus initially on line-by-line analysis of the stimulus act and then identify strategies for entering the new markets. One technology company, for example, found $1 billion in revenue opportunities after embracing an organizational blueprint that stressed expanded partnerships with prime government contractors.

Companies will need to formalize these arrangements by weaving their public-sector and government affairs groups into the process of developing strategy and monitoring its execution. A leading private-equity fund learned some of these lessons quickly. Its first response to the new environment was to have its government affairs team work actively with regulators, but only on issues directly affecting the private-equity industry. The fund soon realized, however, that stimulus expenditures would have dramatic effects, beyond relatively narrow finance industry issues, on many companies in its portfolio. Now it's reorienting and bulking up its government affairs team. Similarly, the government relations unit of a health care company has joined forces with marketing and sales. Realigned incentives and responsibilities are keeping the unit's managers in close contact with both customers and regulators, so that the company can quickly learn how new regulations will affect product design.

In short, the public sector's terrain is expanding dramatically, and the private sector is responding. Companies that move with both speed and deliberation should be able to manage the risks of this transition and to find its opportunities.

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