



Health Care, Chaos, and the Challenge of Chickens in Manhattan

John O'Leary and William D. Eggers | February 24, 2010

The debate surrounding the massive health care system overhaul that has been raging in Washington leaves one thing clear: Redesigning roughly one-seventh of the economy is no simple task. The massive 2,000 page health care reform bills recently passed by both houses of Congress—currently languishing in Scott Brown limbo—represent an ambitious effort to reorder the “rules of the game” in health care in order to achieve dramatically different

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results. The goals of the plan, as described by President Obama in his state of the union address, are to “bring down premiums, bring down the deficit, cover the uninsured, strengthen Medicare for seniors, and stop insurance company abuses.” While these are admirable goals, the challenge for government is to structure a set of relationships, including incentives, to achieve these goals. A reasonable question arises: Is government the best mechanism by which to structure the incentives that control health care?

The problem is that the participants in the health care market generally aren't concerned with achieving the noble goals of these bills. Instead, each participant—doctors, insurance companies, hospitals and individual patients—are more interested in their own narrow interests. This “What's in it for me?” attitude is quite common among mere humans and, and makes the risks of such a massive and complex

reform daunting. Utilizing the government to reorder priorities in the health care system may not be as easy as some think. Get the incentives wrong and the outcomes can be disastrous.

California learned this the hard way when it overhauled its electricity market in the late 1990s. The idea was that the stodgy world of regulated utilities and public monopoly providers would be replaced by “competition,” but competition taking place within the context of a complex new system of rules, including price controls. The goal was lower energy prices, but the result was a disaster. Energy producers such as Enron soon learned how to game the semi-deregulated system, and within a few years California saw skyrocketing prices, rolling blackouts, and consumer losses of upwards of \$40 billion. The price controls inserted into the law to protect consumers didn't work, and indeed were exploited in a way that created bedlam.

The paradox is that chaos creates order, while control can result in chaos. In an effort to control outcomes, free exchange is curtailed and the essential ordering signals of price and profit are lost—leading to misallocation of resources and outcomes that nobody likes.

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Consider: Who is in charge of getting the right number of chickens to Manhattan every day? After all, few chickens live there, but a lot of chickens get eaten there. The typical Manhattanite downs about



sixty pounds of chicken a year, in every imaginable form, from chicken chow mein to chicken nuggets, from organic chicken to those little cubes that float in your can of chicken soup. Untold thousands of people participate in providing for Manhattan's ever-changing chicken needs, from truck drivers to restaurant owners, from grocery store managers to Arkansas chicken farmers. Who is in charge? Who makes sure that New York City winds up with the right amount of the right kind of chicken?

The answer is: No one. The chaos of the uncontrolled buying and selling of the market produces an orderly pattern of exchanges that coordinates the activities of independent yet interdependent participants. The result, without any central planning, is an adaptable and ever-changing arrangement that generally meets the needs of Manhattan's chicken eating public. The government provides certain oversight and context for the market. The U.S. Department of Agriculture watches over chicken farms and the city's Board of Health licenses and inspects restaurants. Chickens are hauled over public roads and contract disputes between chicken farmers and truckers are resolved in public courts. But when it comes to the essence of the chicken delivery system—how much chicken, of what kind, at what price—it is the invisible workings of supply and demand that align the productive activities of a loose network of thousands of people (and companies) in making sure New Yorkers get their chicken potpie, chicken vindaloo, and extra-spicy buffalo chicken wings.

Author Francis Fukuyama believes we are just beginning to understand the paradox of how chaos can create order. In *The Great Disruption* Fukuyama notes that “The study of how order arises, not as the result of top-down mandate by hierarchical authority, whether political or religious, but as the result of self-organization on the part of decentralized individuals,

is one of the most important intellectual developments of our time . . . In an information society, neither governments nor corporations will rely exclusively on formal, bureaucratic rules to organize the people over whom they have authority.”

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In our chicken example, information that shapes behaviors travels through the market through prices. The mind-boggling complexity boils down to a set of choices. How much chicken should I order this week for my restaurant? Should I hire another chicken plucker? How much should we charge for the chicken schwarma? Should I get the chicken marsala for \$14.95 or the veal marsala for \$17.95? Prices and profits give signals to both producers and consumers. There are two areas in which large numbers of people are occupied in productive activities in which they are not exposed to price feedback: large corporations and government. For example, a twenty-person legal department at a corporation generally does not charge an hourly fee to its “internal clients.” In contrast, a twenty-person law firm not only charges its clients, it also keeps a close eye on the difference between resources consumed (costs) and value created (revenue), since the difference between the two will be the firm's profit or loss. It is relatively easy to assess how the law firm is doing and much harder to assess how the legal department is doing.

For both large corporations and government, the problem of alignment—of coordinating the productive activities of individuals—is made more difficult by the absence of monetary measures on outputs. Large corporations enjoy a significant advantage over government because they at least



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get profit feedback in aggregate. You may not know how profitable the legal department is, but at least you know how profitable the company is overall. In government, the lack of a single measure of organizational performance—profit—makes it more challenging for managers to coordinate the activities of those who work within it.

An enduring challenge of the public sector is how to foster alignment, or “goal congruence,” among those who work within it. As the problems the public sector deals with get more complex (such as health care), these challenges will only get bigger. Taking a cue from the corporate world, which struggles with a similar challenge, can provide some valuable lessons here. Throughout the network of unaffiliated participants, everyone is asking the same question about every activity along the way, “What’s in it for me?” The chicken farmer will add capacity only if they can earn a profit on those “incremental” chickens. The truck driver won’t haul your chickens if he can’t make money doing so. The restaurant owner won’t offer chicken pot pie unless people are willing to pay for it. Even the chicken gobbling citizen at the end of the line is searching for a way to fill his belly at a bargain price.

But what about the public sector?

Government does not, cannot, and should not measure itself strictly in terms of dollars and cents. In the for-profit sector both inputs and outputs can be measured in dollars, while in government, inputs are measured in dollars but outputs have to be measured using—and here it gets tricky—something else. Any public activity, from schools to roads to the courts, consumes public resources and delivers a public value. But is the value delivered commensurate with the resources being consumed? That is the essence of “accountability.” In a competitive market, there are

consequences for failing to deliver value, but most government entities lack that sort of harsh feedback. The never-ending search for accountability is the effort to substitute performance measures to take the place of a profit measure.

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There are two major challenges to performance measurement in the public sector. First, judging value is often subjective. Second, linking performance measurement to consequences isn’t all that easy.

The wide variety of chicken offerings in Manhattan exist in part because of the subjective nature of evaluating value. You love the chicken vindaloo at the Indian restaurant across the street, I think it’s too spicy. Who is correct? We both are. The chaos of the market does a remarkable job of discovering and satisfying the varied tastes of consumers. My local supermarket offers 32 different varieties of mustard (Dijon, yellow, brown, honey, etc.) and 11 different kinds of hot dogs, including beef, tofu and chicken dogs. Collectively providing a service, such as education, generally reduces the variety of offerings. Private schools in my area offer Montessori, Waldorf, and religious based instruction, as well as bilingual immersion schools. Some are quite costly, others much less so. In contrast, the local public schools offer much less variety at a single price point.

In addition to subjective evaluation based on individual preferences, public providers lack mechanisms to enforce consequences for poor performance. Let us imagine that through exhaustive measurement we determine that one city’s public schools aren’t performing very well: costs are high, tests scores are



low, etc. What can be done about it? A school district can't go out of business, and it certainly doesn't make sense to withhold funds until it improves—that only punishes the children trapped in dysfunctional schools. The only mechanism for improvement is political pressure on elected leaders, which is a far slower and cumbersome process than the direct and painful feedback of the market which drives underperforming organizations out of business.

The irony is clear: The “Chicken Delivery System” of New York is pure chaos, with no one to complain to if you are unhappy. No one is in charge of getting chickens to Manhattan. But the organized chaos of the market delivers results that often surpass the highly organized public delivery systems in areas such as education and public safety. Indeed, the more complex the task, the harder it is for the highly organized, hierarchical public sector to cost-effectively deliver public value. Remove the information rich signals of price and profit, and you now face the daunting challenge of organizing productive activities in some other way. This isn't an argument for market anarchy, but merely a cautionary tale for those who would seek to expand the authority of government to achieve the public policy outcomes they desire.