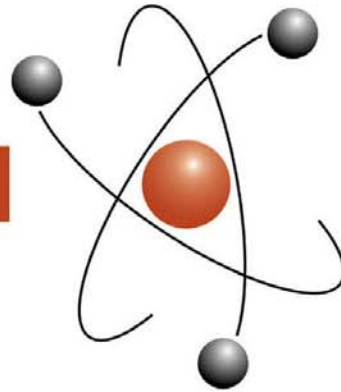


S U S T A I N



A B I L I T Y

ACTUARIES AND THE FUTURE

What Price Health?

**Private Health Insurance cost pressures
and product pricing**

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Health insurance prices in the news

No relief for health premiums

Health funds: pay more and get less More jolts expected as system fails to keep lid on premiums
Double trouble: rates, health premiums up

Gillard attacks premium increases

Cost is a killer issue for family health cover

Health at too high a premium

Technology takes 50pc of health spending

Private health costs to rise

Health-fund premiums to rise

Cost of health cover to soar

Health costs us an arm and a leg

Rises could force out young

Health fund pain tipped

Propping up a costly private health system

Outrage over 18pc health cover rise



Outline

- **Cost pressures**
 - **Hospital**
 - **Medical**
 - **Ancillary**
 - **Ageing**
- **Industry Profitability**
- **Price Increases – Industry, Fund**
- **Product choice**
- **Prices in the market**
- **Pricing dilemma: product design vs claims experience**
- **Discussion**



Cost Pressures

Year ended	% increase in Benefits paid per SEU over previous year	
	Hospital	Ancillary
Dec 97	4.9%	3.5%
Dec 98	4.4%	1.6%
Dec 99	0.6%	6.1%
Dec 00	-14.4%	-1.1%
Dec 01	7.6%	13.5%
Dec 02	12.3%	13.8%
Dec 03	9.3%	0.8%
Dec 04	9.0%	1.3%
3 years to Dec 04	10.2% pa	5.1% pa

- Hospital benefits per SEU growth $\cong 4 \times \text{CPI}$
- Ancillary benefits per SEU growth $\cong 2 \times \text{CPI}$
- Ancillary benefits affected by growth, then removal, of “lifestyle” benefits



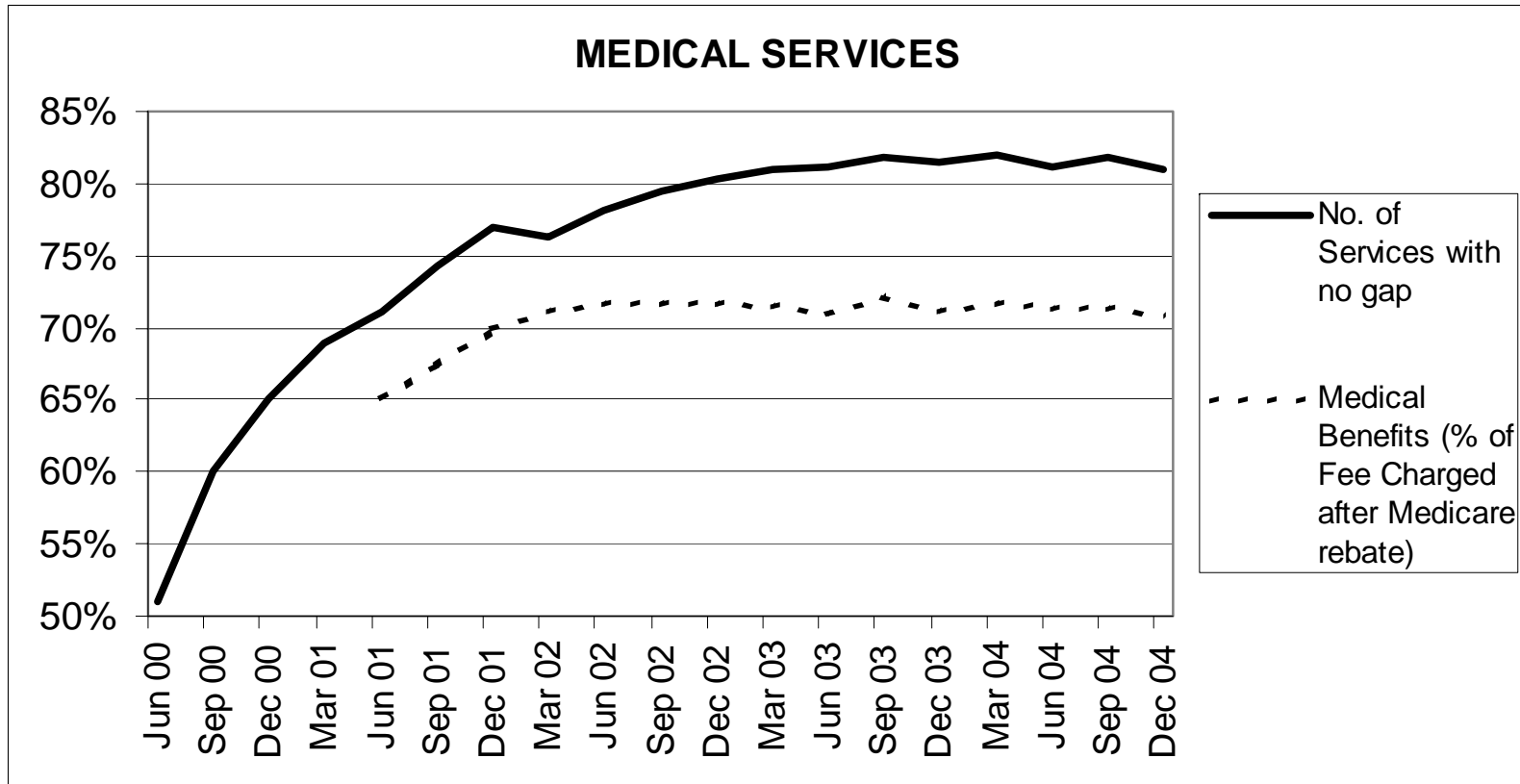
Cost Pressures: Hospital

Year ended	% increase in Hospital Benefits paid per SEU over previous year		
	Accommodation	Medical	Prostheses
Dec 97	3.7%	3.7%	27.3%
Dec 98	2.7%	9.2%	22.5%
Dec 99	-1.1%	9.4%	11.0%
Dec 00	-16.0%	1.4%	-14.2%
Dec 01	4.0%	29.7%	16.6%
Dec 02	7.6%	30.4%	28.8%
Dec 03	6.5%	10.7%	28.4%
Dec 04	6.8%	13.0%	18.0%
3 years to Dec 04	7.0% pa	17.7% pa	25.0% pa

- **Rapid growth areas are prostheses and medical – has this abated?**
- **Prospects for lower accommodation benefits growth? - contracting**



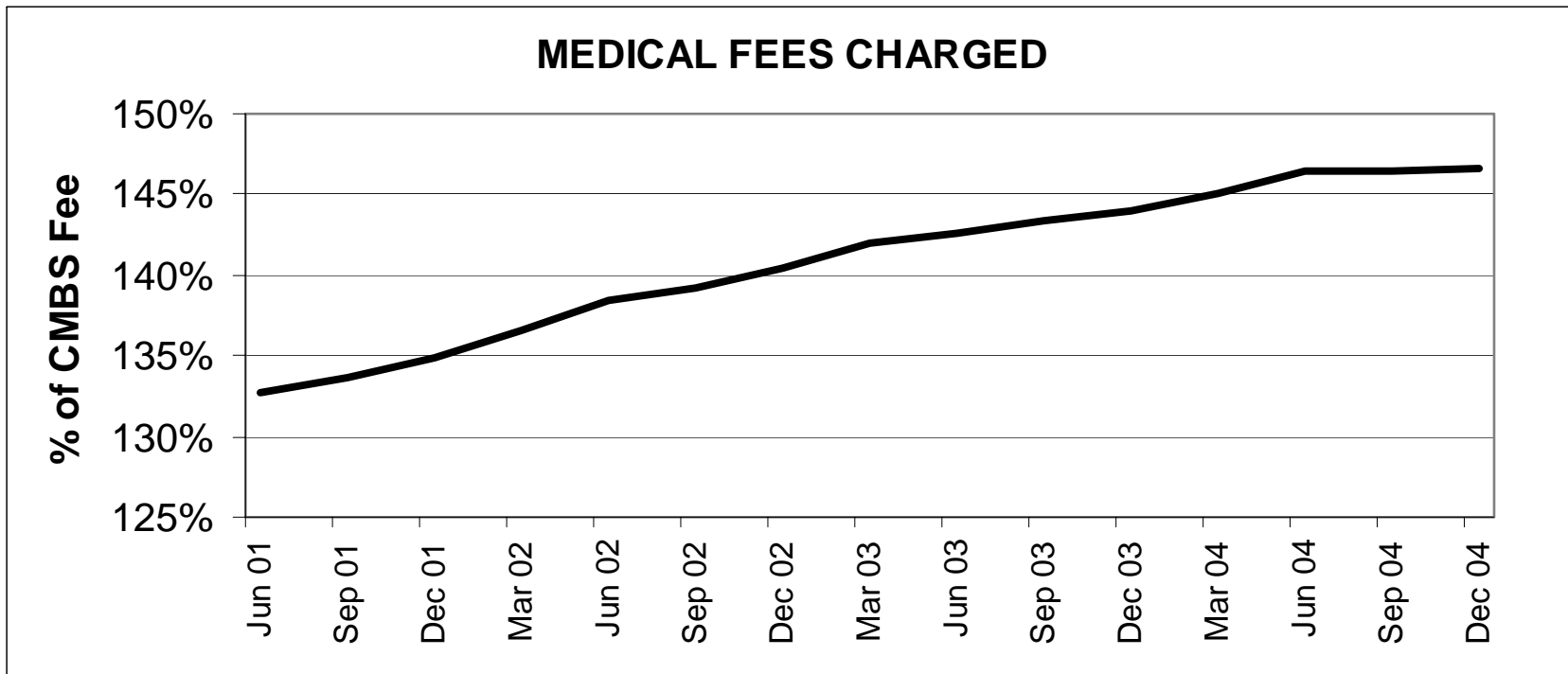
Cost Pressures: Medical



- **No Gap coverage of medical services has reached saturation**
- **Any further increase in coverage will be expensive – largest gaps remain**



Cost Pressures: Medical



- **Medical Fee increases: did fees increase in response to fund contracting?**
- **Has fund contracting stabilised fee levels relative to CMBS?**



Cost Pressures: Ancillary

Year ended	% increase in Ancillary Benefits paid per SEU over previous year				
	Dental	Optical	Physiotherapy	Chiropractic	Other
Dec 97	4.2%	5.1%	-0.1%	3.0%	1.0%
Dec 98	1.9%	0.3%	4.7%	2.2%	-0.2%
Dec 99	3.8%	6.3%	10.4%	7.4%	12.2%
Dec 00	-4.7%	5.7%	-0.5%	1.8%	3.2%
Dec 01	13.9%	11.8%	10.8%	12.6%	15.8%
Dec 02	7.3%	10.4%	10.0%	7.7%	42.7%
Dec 03	0.9%	3.4%	1.2%	0.4%	-1.7%
Dec 04	4.1%	3.6%	3.3%	3.9%	-9.5%
3 years to Dec 04	4.1% pa	5.8% pa	4.8% pa	3.9% pa	8.3% pa

- **Benefit growth per SEU in most major benefit categories \cong 1 to 2 x CPI**
- **Other category affected by popularity of “lifestyle” benefits in 2001-02 and removal in 2003**



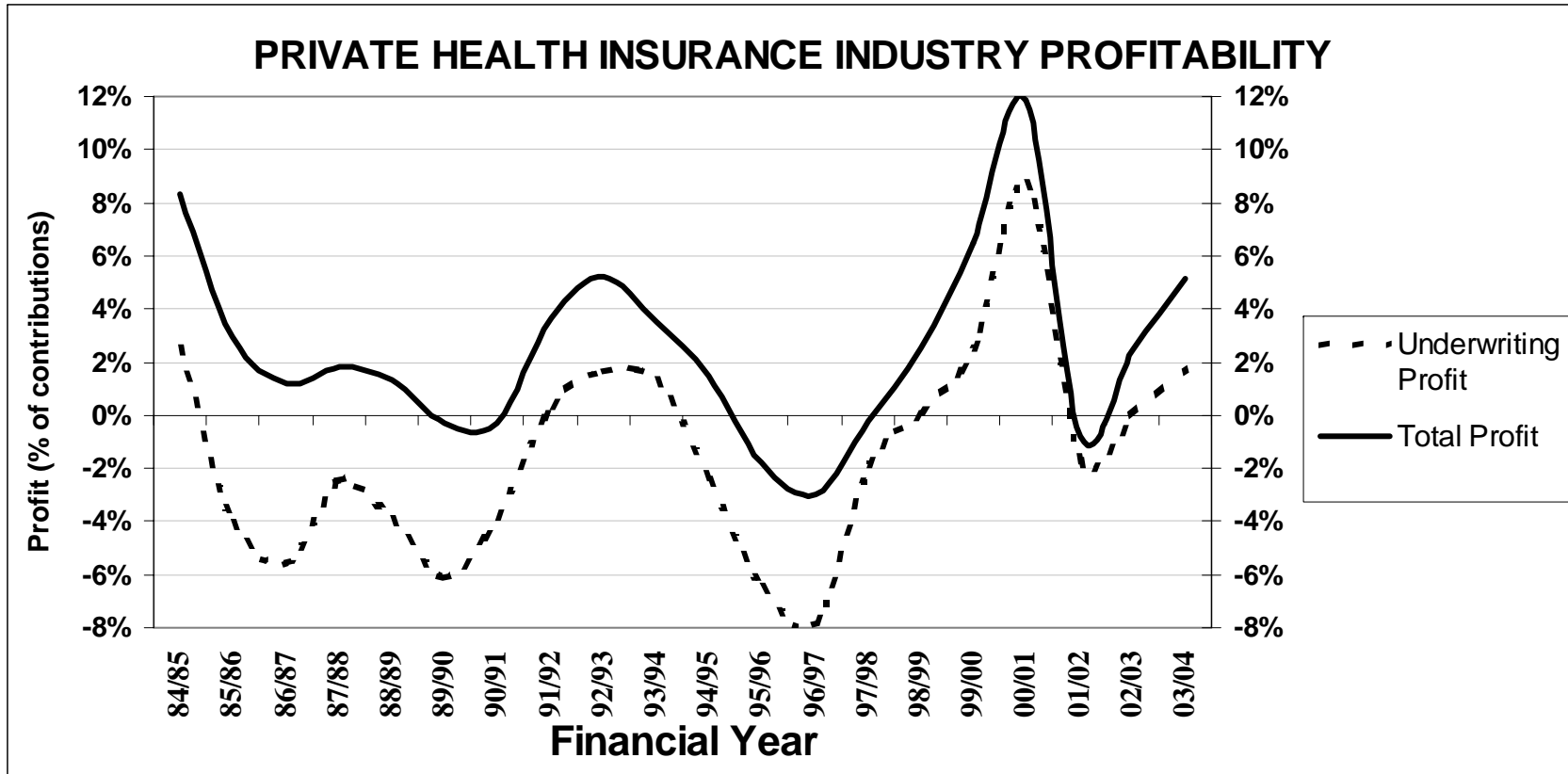
Cost Pressures: Ageing

Year ended	Hospital Insurance Risk Profile change	Change in Hospital Persons Covered
Dec 98	1.9%	-3.6%
Dec 99	-1.1%	5.2%
Dec 00	-12.0%	46.4%
Dec 01	1.9%	0.2%
Dec 02	1.9%	-0.5%
Dec 03	1.9%	-0.3%
Dec 04	1.9%	0.2%

- **Changes in the age profile of the PHI population has consistently led to hospital benefit increases of 1.9% per annum**
- **Impact of Rebate/Lifetime Health Cover in 1999 and 2000**



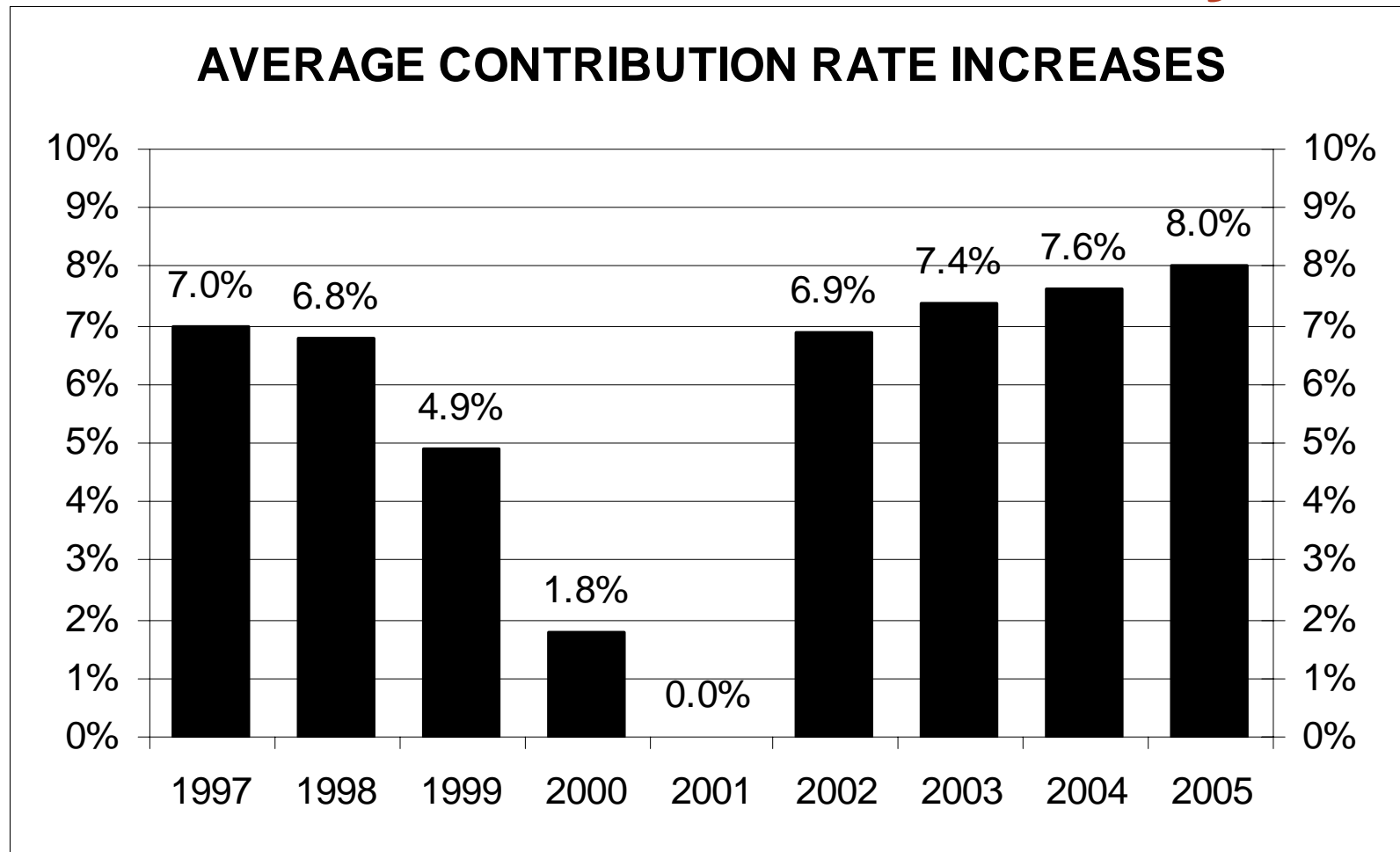
Industry Profitability



- 20 year averages: Underwriting Margin -1.3% ; Total Profit Margin 2.6%
- Estimated that a margin of 2.5% is required to maintain Capital Adequacy



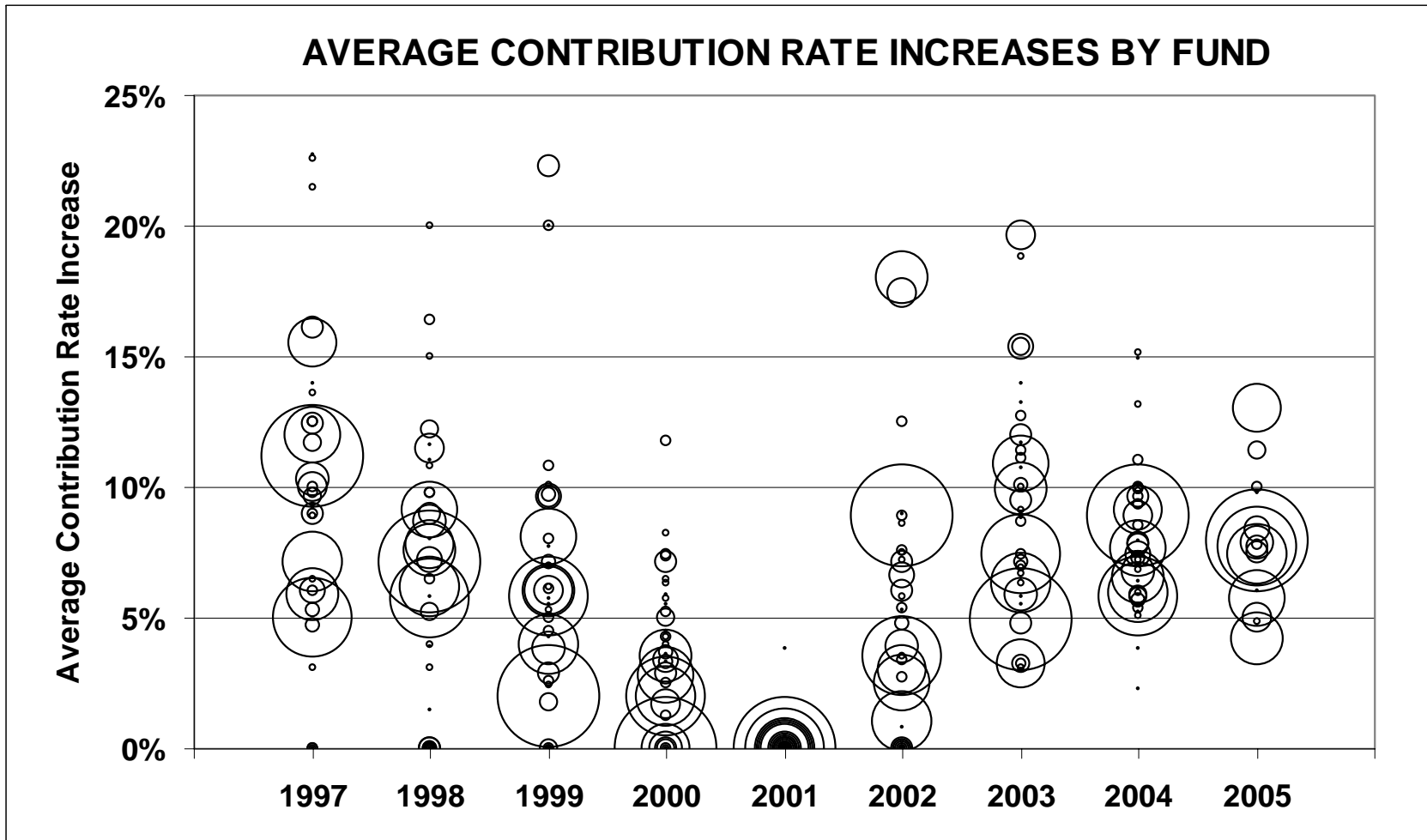
Price Increases: Industry



- Industry average contribution rate increase has consistently been 7% - 8%
- Exception was immediately before and after start of Lifetime Health Cover



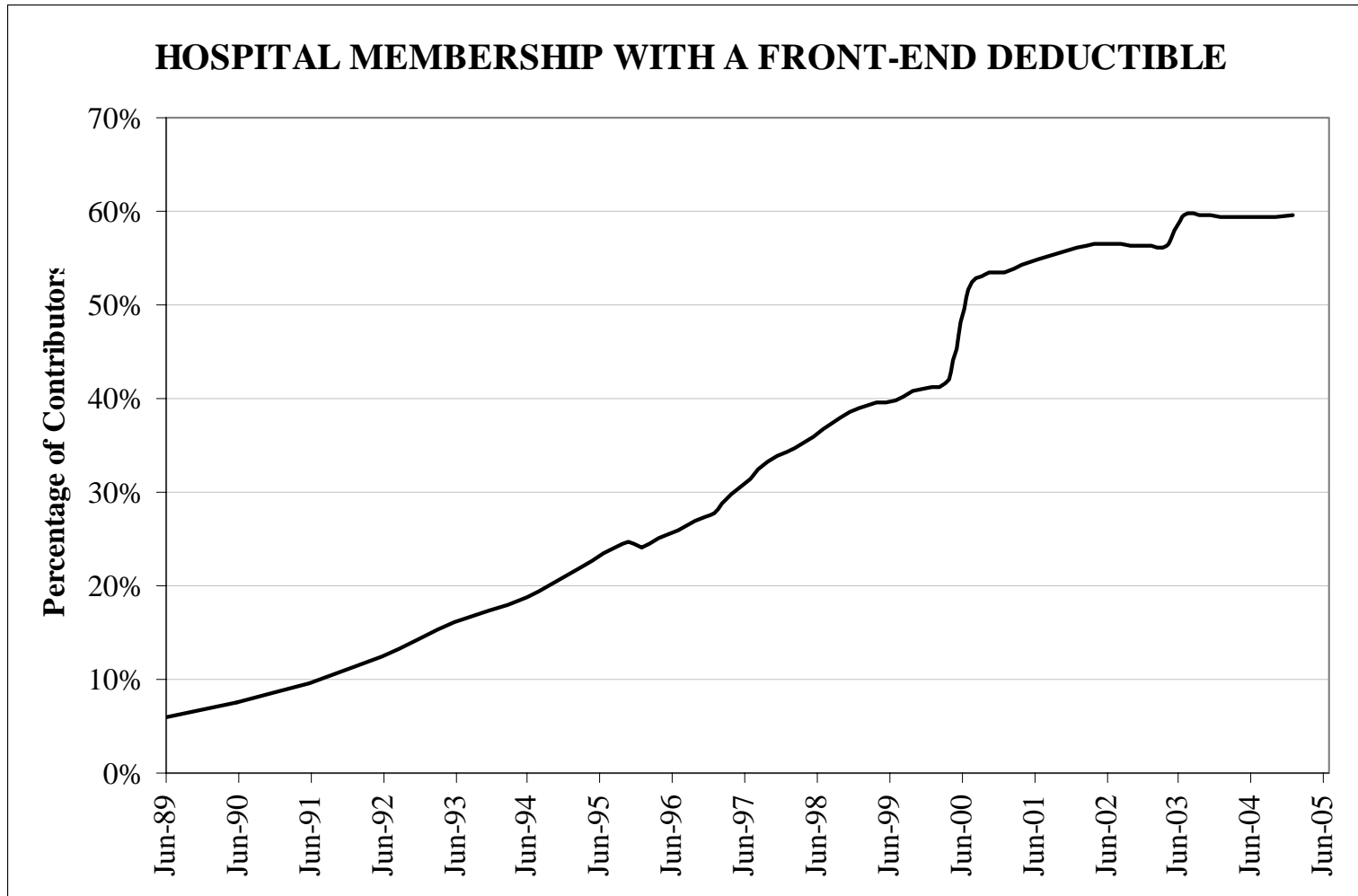
Price Increases: by fund



- Wide variation in average increase between funds
- Narrowing range in recent years?



Product Choice



- **FEDs allowed in 1985: increased from 30% in 1997 to 60% in 2004**



Product Choice

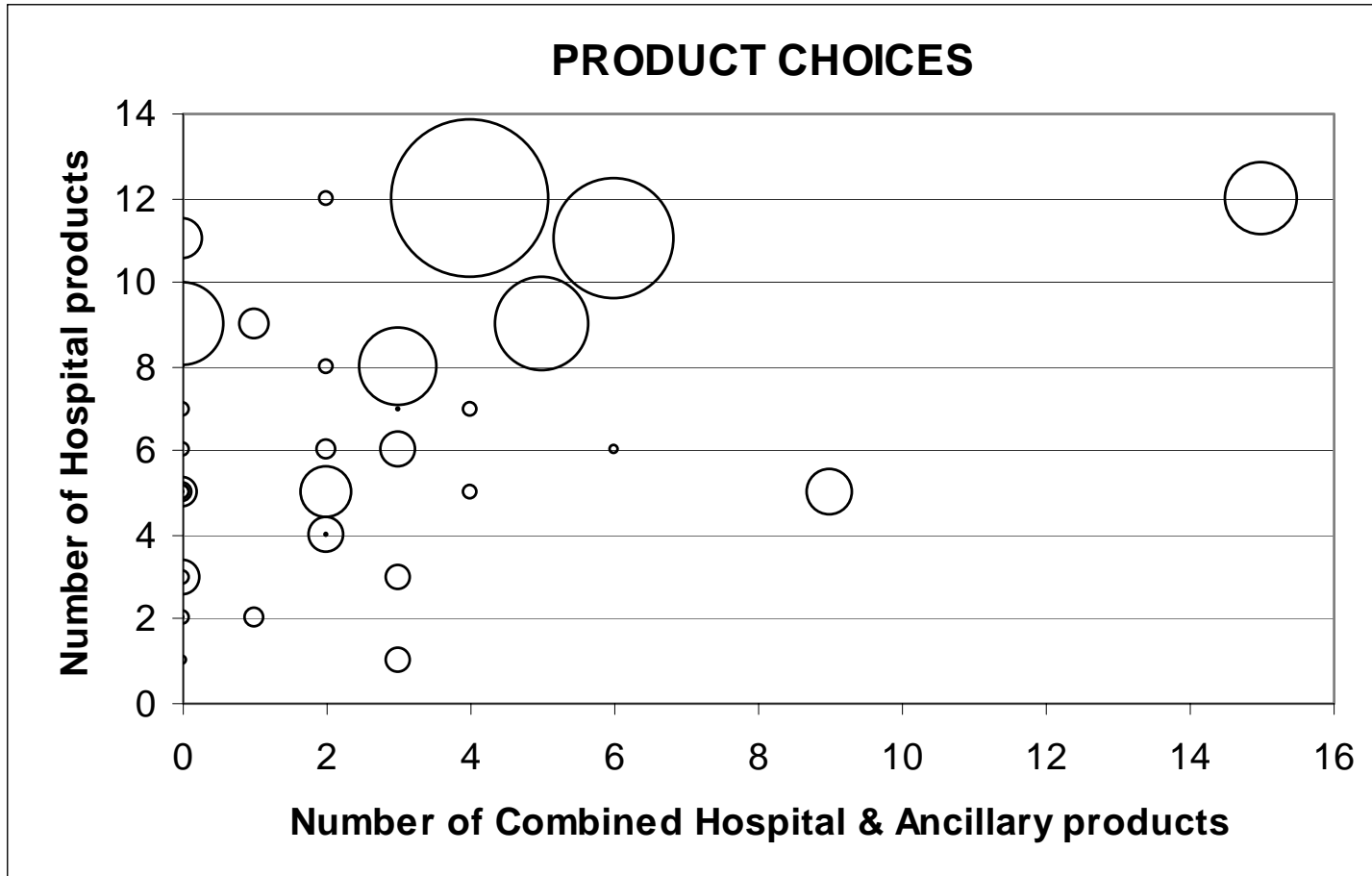
Product Type	No Exclusions	With Exclusions	Total
Full cover	63%	1%	65%
Restricted cover	33%	3%	35%
Total	96%	4%	100%

Excess/Co-Payment Level per annum	% of contributors
Nil	27%
Up to \$500 Single / \$1000 Family	54%
Over \$500 Single / \$1000 Family	19%

- **63% of members have full cover ie. no restrictions or exclusions**
- **37% of members have either products with benefit restrictions or exclusions**
- **73% of members have some form of member moiety (FED,excess,co-payment)**

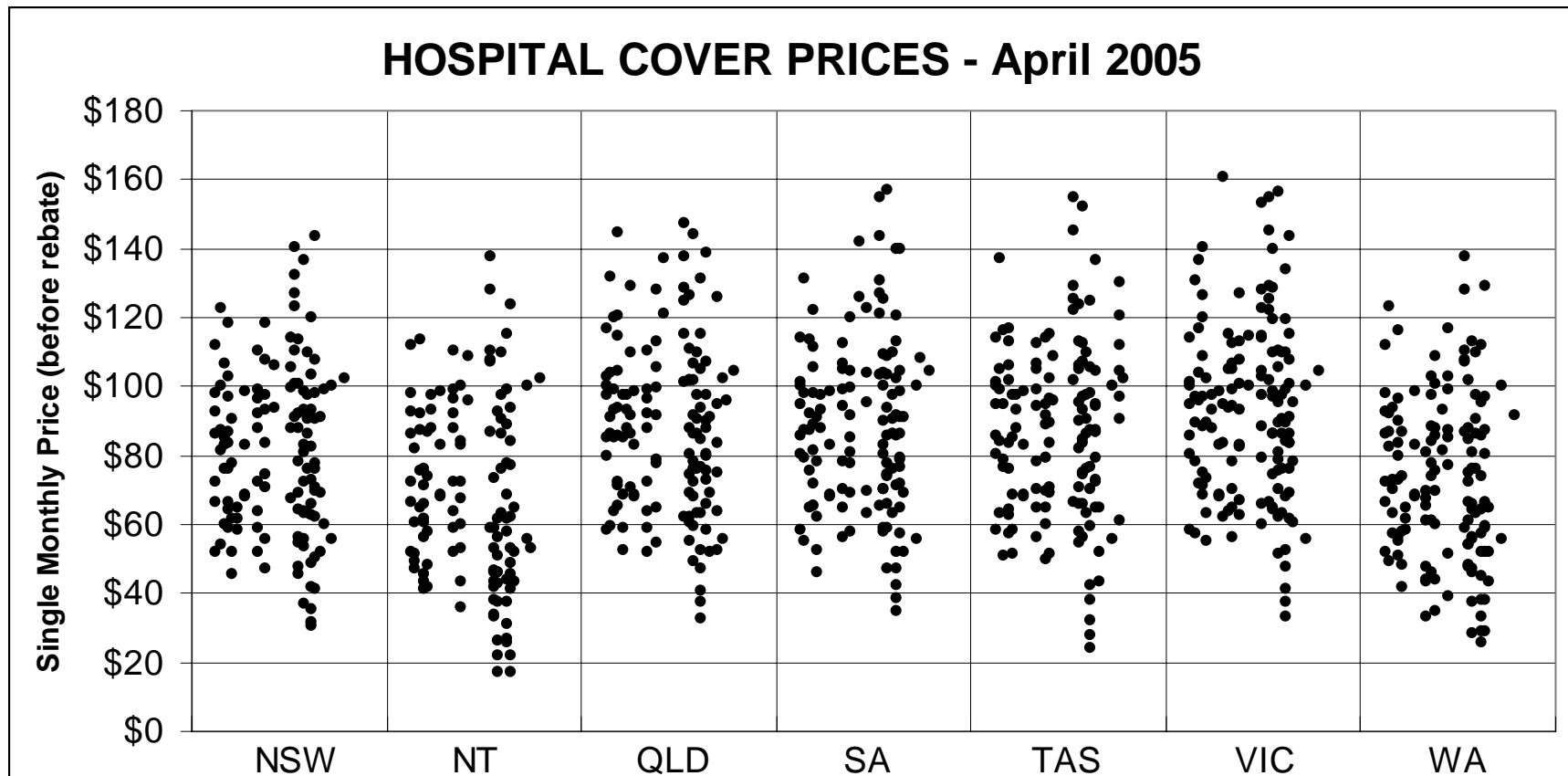


Product Choice



- Number of product choices on offer generally increases with size of fund

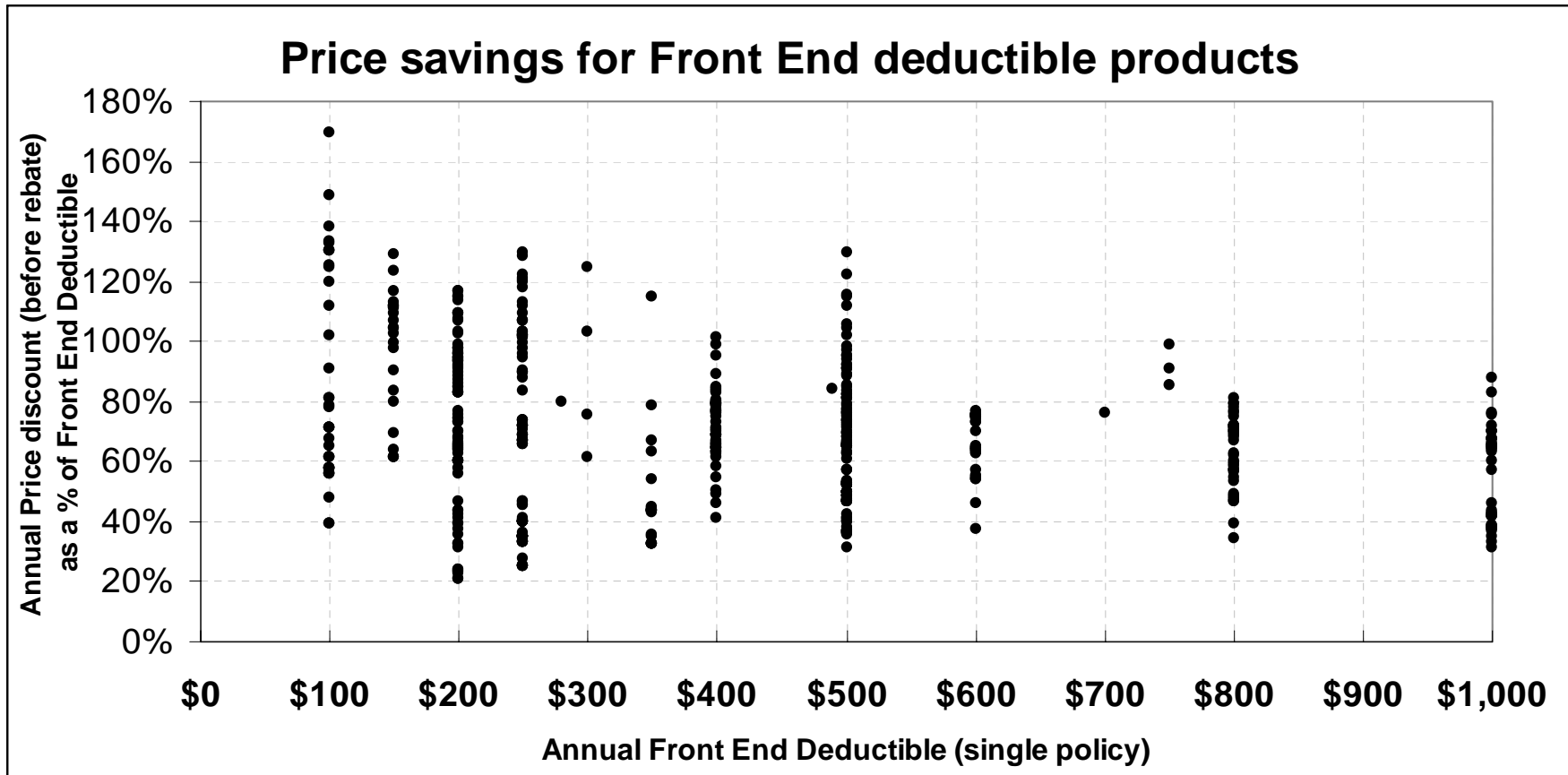
Prices in the Market



- Survey of hospital prices for 32 funds (May 2005 prices)
- Price of hospital cover varies between \$20 and \$160 per month (single)

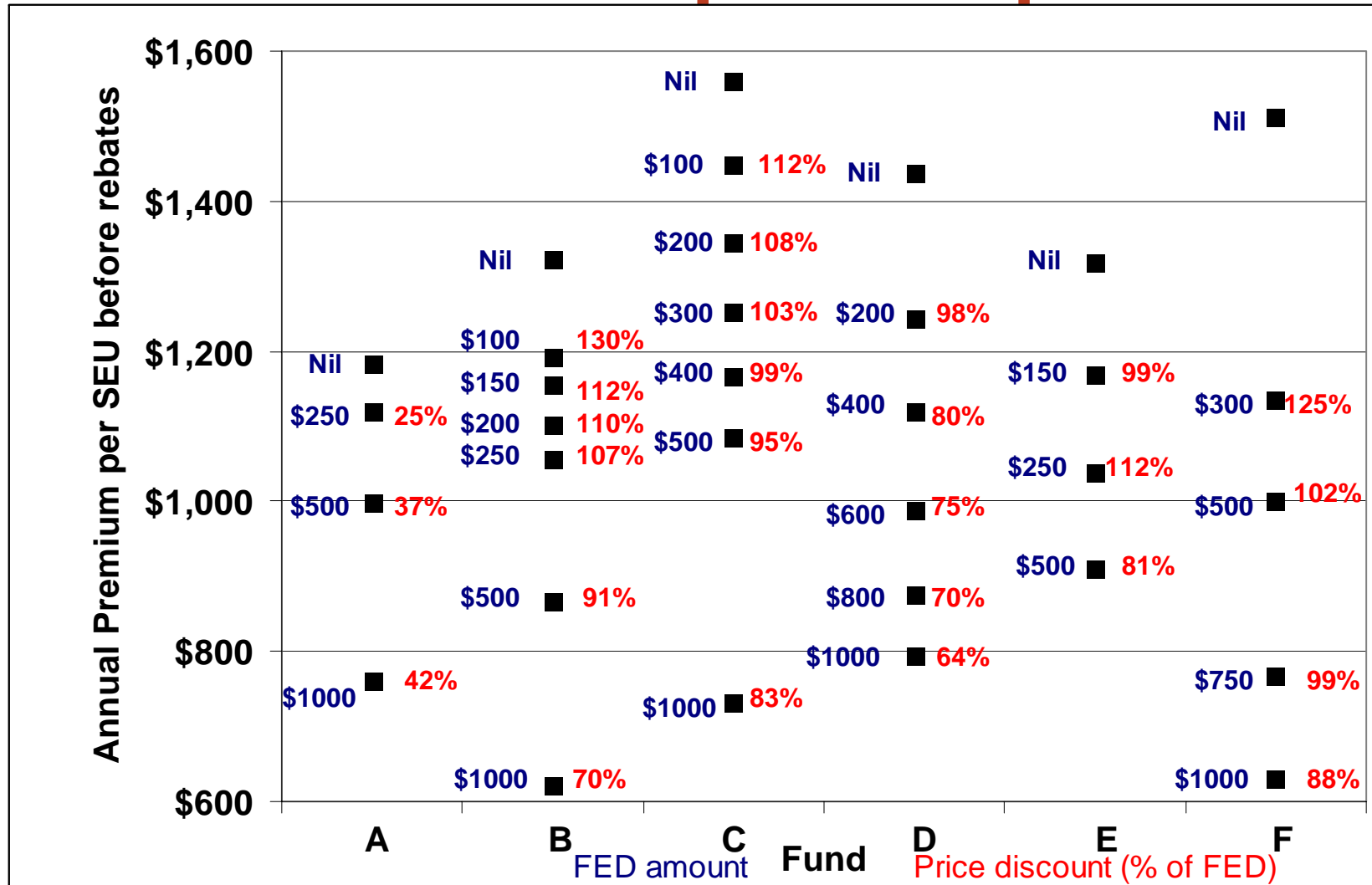


Prices in the Market: FED pricing



- **Wide variation in pricing approaches across the industry**
- **Reliance on inertia and ignorance of members?**
- **Explicit/Implicit cross subsidisation decisions?**

A selection of product prices



- Products are not necessarily directly comparable between funds
- Not all funds are from the one state



Prices in the Market: Too cheap?

State	Minimum Cost = Reinsurance Levy plus Ambulance Levy pa per SEU year ended Dec 2004	Cheapest Product in Market per SEU pa (before rebate) at April 2005	Margin to cover claims, expenses and profit (% of contributions)
NSW	\$347*	\$364	4.7%
NT	\$93	\$205	54.6%
QLD	\$372	\$392	5.1%
SA	\$358	\$417	14.1%
TAS	\$371	\$287	(29.3%)
VIC	\$365	\$397	8.1%
WA	\$276	\$310	11.0%

- **Minimum cost = Reinsurance Deficit per SEU + Ambulance Levy**
- **Based on prices in the market, some cheap products must be loss making**



Pricing dilemma: product design vs claims experience

per SEU per annum	Hospital Product A	Hospital Product B	Hospital Product C
Annual FED	Nil	\$200	\$400
FED collected	0	50	70
Claims paid	2350	1800	900
Reinsurance payt/(recpt)	-900	-600	100
Net Claims Cost	1450	1200	1000
Price	1600	1450	1300
Price discount (% of FED)		75%	75%
Gross Margin	9%	17%	23%
Price for 13% margin	1667	1379	1149
Price discount (% of FED)		144%	129%

- **Should the price of product A be increased, despite the cannibalisation risk?**



Discussion Points

- **Is Community Rating dead?**
- **Is it necessary to break down Community Rating in order to support it?**
- **How should funds respond to adverse selection and its disparate margin outcomes**
- **Should funds voluntarily cross-subsidise between products**
- **How to respond to the pricing dilemma: striking a balance between product design and claims experience**
- **Potential for product cannibalisation**
- **Is it possible to redesign the risk adjustment scheme to adequately respond to adverse selection?**