

The Future of Medicare Supplement

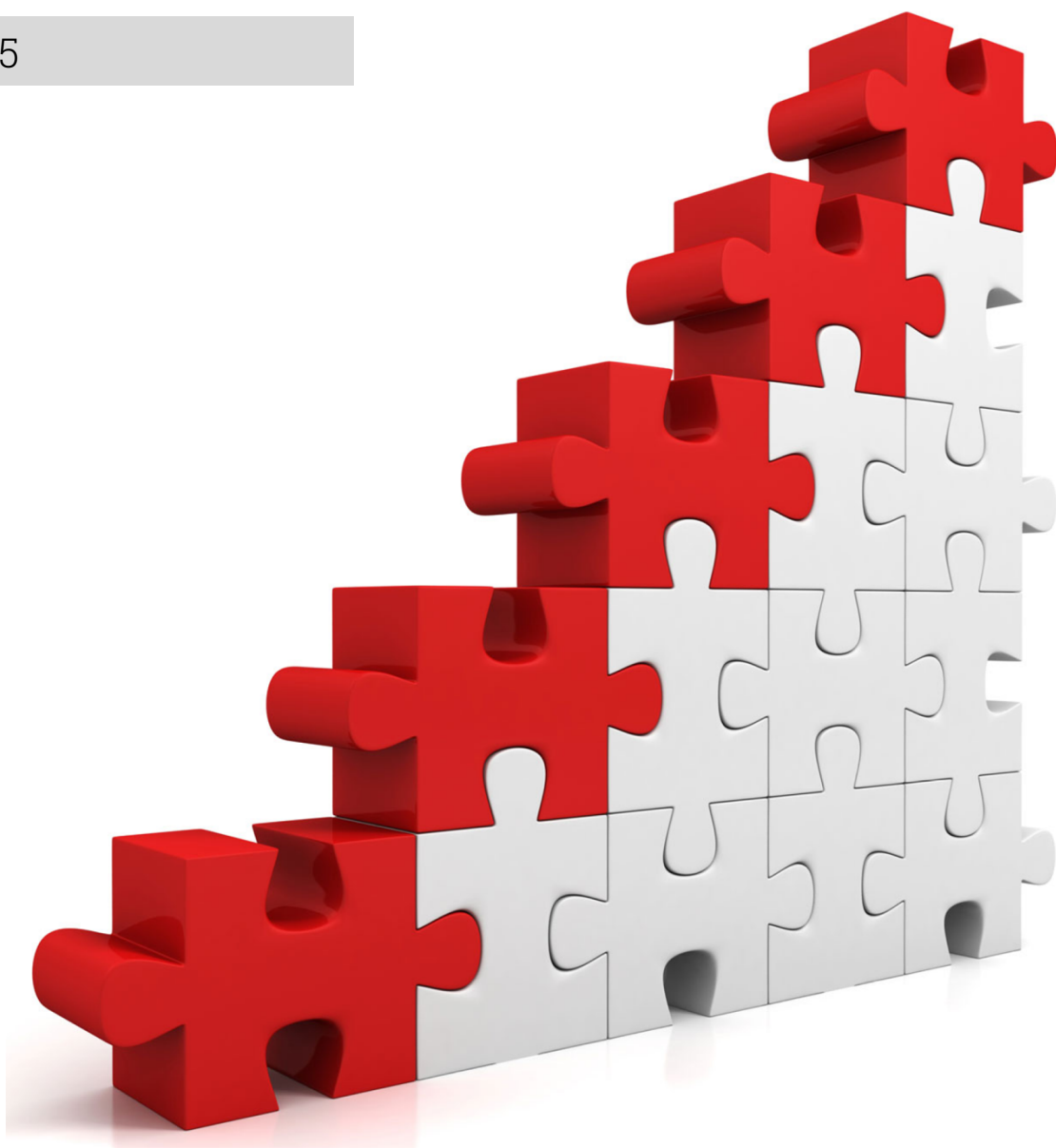
5th Annual Market Projection

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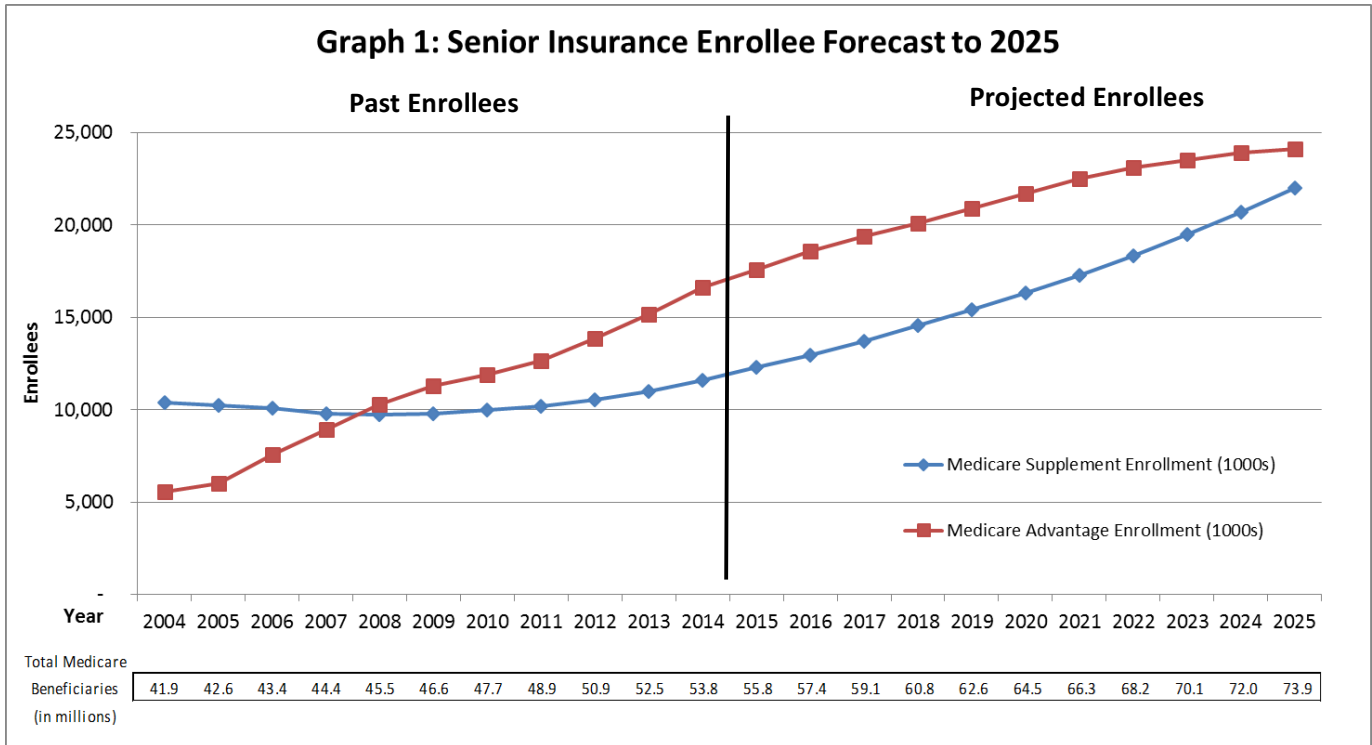
3rd Quarter 2015



Introduction

The Medicare Supplement market continues to offer long-term sustainability. Almost 74 million individuals are expected to be enrolled in the Medicare program by 2025 (a 37% increase over 2014).

CSG Actuarial research indicates Medicare Supplement enrollments will continue to grow markedly over the next 10 years, creating ever-increasing opportunities for insurance carriers, agents, and marketing organizations in the Medicare Supplement market (Graph 1).



Methodology

There is a minimal amount of information available regarding Medicare Supplement market projections. CSG Actuarial has compiled data from various sources and developed actuarial models to project future Medicare Supplement enrollments and premium levels over the next 10 years.

Current Medicare Eligibility Assessment

To determine how Medicare Supplement would grow over the next 10 years, we first evaluated the current Medicare population using the following demographic factors:

- Age
- Eligibility Status
- Gender
- Income Level
- Area of Residence
- Living Arrangement
- Plan Type (Medicare Supplement, Medicare Advantage, Other)

Table 1 provides a current percentage snapshot of each of these characteristics used in our projection.

Table 1						
Medicare Beneficiary Data (in 1000s) - 2014						
Category	All Enrollees		Medicare Supplement		Medicare Advantage	
	Number	% Dist	Number	% Dist	Number	% Dist
Total Enrollment	53,826		11,572		16,632	
Eligibility Status						
Aged	44,799	83.2%	11,210	96.9%	14,468	87.0%
Disabled	9,027	16.8%	363	3.1%	2,164	13.0%
Age						
Under 45 Years	2,170	4.0%	33	0.3%	309	1.9%
45-64 Years	6,857	12.7%	330	2.9%	1,854	11.2%
65-74 Years	24,354	45.2%	5,820	50.3%	7,975	48.0%
75-84 Years	15,100	28.1%	3,540	30.6%	4,802	28.9%
85 Years or Older	5,345	9.9%	1,849	16.0%	1,693	10.2%
Gender						
Male	24,410	45.4%	4,899	42.3%	7,202	43.3%
Female	29,416	54.7%	6,674	57.7%	9,430	56.7%
Annual Income						
\$10,000 or Less	7,724	14.4%	446	3.9%	2,157	13.0%
\$10,001-\$20,000	13,952	25.9%	2,010	17.4%	4,449	26.8%
\$20,001-\$30,000	9,947	18.5%	2,306	19.9%	3,265	19.6%
\$30,001-\$40,000	12,079	22.4%	3,319	28.7%	4,012	24.1%
\$40,001 or More	10,125	18.8%	3,492	30.2%	2,751	16.5%
Area of Residence						
Urban	41,150	76.5%	8,025	69.3%	14,432	86.8%
Rural	12,676	23.6%	3,547	30.7%	2,200	13.2%
Living Arrangement						
Lives Alone	16,234	30.2%	3,460	29.9%	4,795	28.8%
With Spouse	30,622	56.9%	6,802	58.8%	8,607	51.8%
With Children	4,128	7.7%	753	6.5%	1,823	11.0%
With Others	2,842	5.3%	558	4.8%	1,407	8.5%

Sources: 2015 Medicare Trustees Report and the 2012 Medicare Beneficiary Survey

Disclaimer: Limited information was available for some of the categories and certain assumptions have been made based on analysis of the data.

Medicare Eligibility Projection

Table 2 features the overall Medicare beneficiary projection. The growth projected by the 2015 Medicare Trustees Report is being driven by the well-documented influx of baby boomers now turning 65 and joining the Medicare program.

Table 2		
Year	Total Medicare Beneficiaries	% Increase By Year
	(1000s)	
2004	41,902	
2005	42,606	1.7%
2006	43,436	1.9%
2007	44,368	2.1%
2008	45,500	2.6%
2009	46,604	2.4%
2010	47,720	2.4%
2011	48,896	2.5%
2012	50,874	4.0%
2013	52,481	3.2%
2014	53,826	2.6%
2015	55,829	3.7%
2016	57,404	2.8%
2017	59,067	2.9%
2018	60,818	3.0%
2019	62,619	3.0%
2020	64,471	3.0%
2021	66,335	2.9%
2022	68,246	2.9%
2023	70,145	2.8%
2024	72,001	2.6%
2025	73,890	2.6%

Source: 2015 Medicare Trustees Report

Historical Medicare Supplement Assessment

To project the future of the Medicare Supplement market, we started by evaluating historical trends. Table 3 indicates that Medicare Supplement policies in-force and premiums have rebounded in the past six years, fueled by an increase of annualized new premiums, which are up 64% since 2008. The increase in annualized new business premiums has driven a leveling of the Medicare Supplement market penetration percentage since 2009, followed by an increase in 2013 and 2014.

Table 3					
Historical Medicare Supplement #'s (in 1000s)					
Year	Total Policies Inforce	Total Premium	Average Premium	% of Medicare Beneficiaries	New Annualized Premium
2004	10,370	18,706,808	1,804	24.7%	2,000,000
2005	10,254	19,339,544	1,886	24.1%	2,100,000
2006	10,078	19,018,522	1,887	23.2%	2,100,000
2007	9,791	19,067,408	1,947	22.1%	2,100,000
2008	9,721	19,588,131	2,015	21.4%	2,200,000
2009	9,767	20,237,384	2,072	21.0%	2,500,000
2010	9,963	21,148,239	2,123	20.9%	2,850,000
2011	10,199	22,106,005	2,167	20.9%	2,850,000
2012	10,549	23,142,217	2,194	20.7%	3,100,000
2013	10,987	24,312,519	2,213	20.9%	3,350,000
2014	11,572	25,732,303	2,224	21.5%	3,600,000

The growth in the Medicare Supplement market during the past six years can mostly be attributed to three things:

1. **The number of Medicare enrollees has grown by almost 18%** (Table 2).
2. **Growth in the Medicare Advantage program has slowed**, which left more lives in traditional Medicare with the need to purchase a Medicare Supplement plan. The average growth rate for Medicare Advantage plans over the past six years is less than half the Medicare Advantage growth rate over the previous three years and has coincided with an increase in the Medicare Supplement growth rate over that same time period (Table 4).
3. **Employers have continued to remove Medicare-aged retirees from their employer health plans**, while providing them with stipends to purchase individual coverage. Due to this, the percentage of Medicare enrollees not in Medicare Advantage or Medicare Supplement plans has declined dramatically the past 10 years (Table 5).

Table 4						
Historical Medicare Advantage & Medicare Supplement Growth - #s in 1000s						
Year	Medicare Advantage			Medicare Supplement		
	Beneficiaries	Annual Growth Rate	Average Growth Rate	Beneficiaries	Annual Growth Rate	Average Growth Rate
2005	6,005			10,254		
2006	7,557	25.8%		10,078	-1.7%	
2007	8,933	18.2%	19.7%	9,791	-2.8%	-1.8%
2008	10,283	15.1%		9,721	-0.7%	
2009	11,303	9.9%		9,767	0.5%	
2010	11,885	5.1%		9,963	2.0%	
2011	12,628	6.3%	8.4%	10,199	2.4%	3.0%
2012	13,877	9.9%		10,549	3.4%	
2013	15,146	9.1%		10,987	4.2%	
2014	16,632	9.8%		11,572	5.3%	

Table 5				
Historical non-Med Adv & Med Supp Market Penetration - #s in 1000s				
Year	Total Medicare	Med Adv & Med Supp	Other	Other % of Total
2004	41,902	15,941	25,961	62.0%
2005	42,606	16,260	26,346	61.8%
2006	43,436	17,635	25,801	59.4%
2007	44,368	18,724	25,644	57.8%
2008	45,500	20,004	25,496	56.0%
2009	46,604	21,070	25,534	54.8%
2010	47,720	21,848	25,872	54.2%
2011	48,896	22,827	26,069	53.3%
2012	50,874	24,426	26,448	52.0%
2013	52,481	26,133	26,348	50.2%
2014	53,826	28,204	25,622	47.6%

These factors and our expectation of the degree to which they would continue were included in the development of CSG Actuarial's Medicare Supplement market projection.

Medicare Supplement Projection

CSG Actuarial's Medicare Supplement projection is featured in Table 6, following. Assumptions include:

- Demographics of current Medicare Beneficiaries are accurate
- Demographics of future Medicare Beneficiaries will not experience a material change in the future
- Mortality rates will follow the 2000 U.S. life table (including mortality improvements)
- Current policy lapse rate and replacement rates will not experience a material change in the future
- Annual Medicare Supplement claim and rate increase trends will not experience material changes in the future
- Structure of Medicare and Medicare Supplement plans will continue as currently designed

Also considered in this projection were the effect of trends in Medicare Advantage, retiree health benefits, and other types of supplemental coverage.

Table 6					
Historical and Projected Medicare Supplement #'s (in 1000s)					
Year	Total Policies Inforce	Total Premium	Average Premium	% of Medicare Beneficiaries	New Annualized Premium
2004	10,370	18,706,808	1,804	24.7%	2,000,000
2005	10,254	19,339,544	1,886	24.1%	2,100,000
2006	10,078	19,018,522	1,887	23.2%	2,100,000
2007	9,791	19,067,408	1,947	22.1%	2,100,000
2008	9,721	19,588,131	2,015	21.4%	2,200,000
2009	9,767	20,237,384	2,072	21.0%	2,500,000
2010	9,963	21,148,239	2,123	20.9%	2,850,000
2011	10,199	22,106,005	2,167	20.9%	2,850,000
2012	10,549	23,142,217	2,194	20.7%	3,100,000
2013	10,987	24,312,519	2,213	20.9%	3,350,000
2014	11,572	25,732,303	2,224	21.5%	3,600,000
2015	12,277	27,325,706	2,226	22.0%	3,900,000
2016	12,966	28,886,213	2,228	22.6%	4,200,000
2017	13,730	30,615,111	2,230	23.2%	4,500,000
2018	14,583	32,540,967	2,231	24.0%	4,800,000
2019	15,442	34,482,206	2,233	24.7%	5,000,000
2020	16,344	36,497,832	2,233	25.4%	5,100,000
2021	17,277	38,607,407	2,235	26.0%	5,400,000
2022	18,336	41,001,344	2,236	26.9%	5,800,000
2023	19,504	43,644,929	2,238	27.8%	6,100,000
2024	20,690	46,331,339	2,239	28.7%	6,400,000
2025	22,014	49,330,643	2,241	29.8%	6,900,000

Current Market Activity and Possible Impacts to Future Medicare Supplement:

Consolidation

The Medicare Supplement market has seen recent activity in mergers and acquisitions with Aetna purchasing Humana, and Anthem purchasing Cigna Corp. It is expected that there will be significant regulatory scrutiny before these deals could become official. While this consolidation will no doubt increase Aetna's and Anthem's market share in the Medicare Supplement market, we don't believe these mergers will create additional or new barriers in the market for other companies.

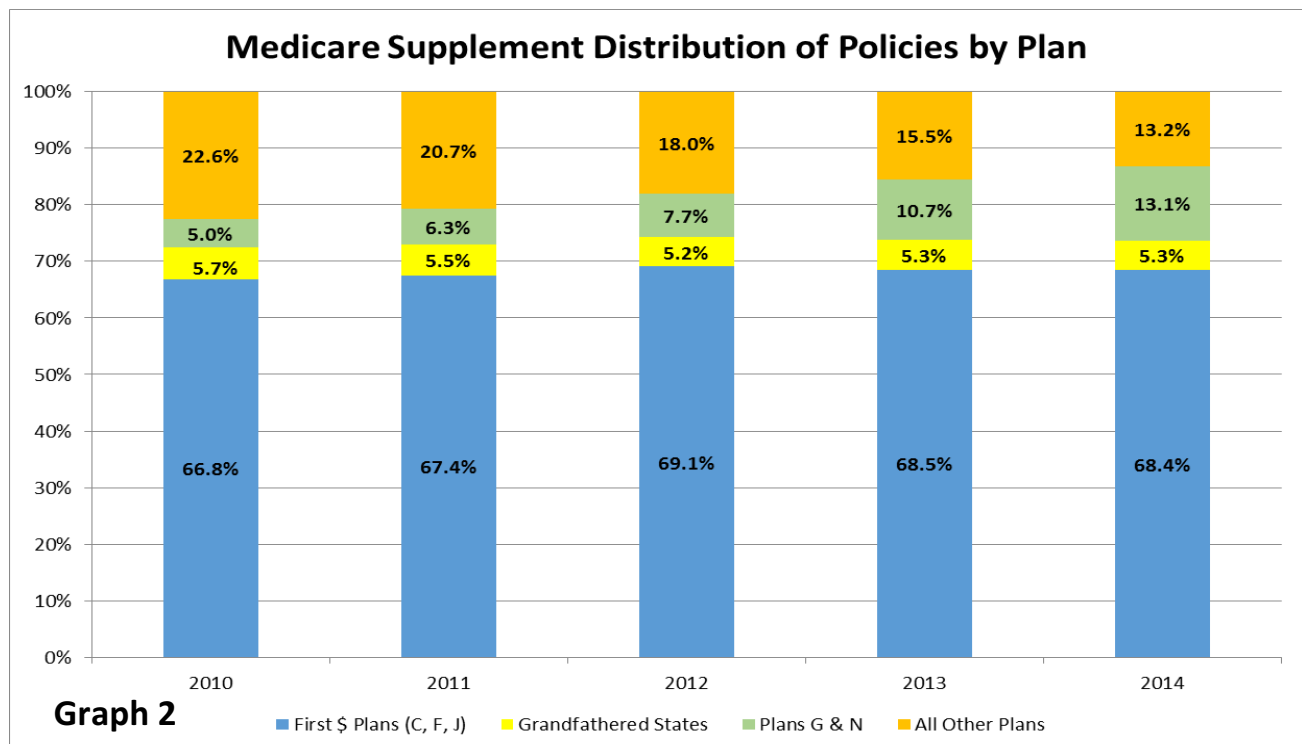
CSG Actuarial does not believe this potential consolidation will negatively impact the growth in the market. We expect there will continue to be new carriers entering the market based on the favorable demographics and cost effective TPA solutions, sophisticated distribution options and reinsurers actively looking for opportunities for new partnerships.

Cost Sharing Plans and First Dollar Coverage

As commonly reported, Plans G and N continue to grow and grab market share in the overall Medicare Supplement market. In 2014 Plans G and N made up over 13% of the lives in the Medicare Supplement market, up from only 5% in 2010.

A common misperception is that the growth of Plans G and N represents a market shift away from plans covering first dollar benefits (primarily plans C and F). The chart (Graph 2) below shows that not to be the case. Using data from the NAIC, CSG Actuarial grouped the Medicare Supplement lives for 2010 to 2014 into 4 categories:

1. Plans covering first dollar benefits (Plans C, F, and J)
2. Plans in Grandfathered States
3. Plans G and N
4. All Other Plans



First dollar coverage plans continue to be the most popular plans in the Medicare Supplement markets.

With the passage of “H.R.2 – Medicare Access and CHIP Reauthorization Act of 2015” Medicare Supplement policies will no longer be able to cover the Part B deductible as part of their benefits beginning January 1, 2020 for newly eligible Medicare Beneficiaries, thus eliminating first dollar coverage plans. There is still much to be determined with the new law as a new NAIC model regulation will be developed and each state DOI will need to update their regulations. There are still questions as to whether plan F will be sold after 2020 to individuals who were eligible prior to 2020? Will plan F and plan G continue to have varying guarantee issue rules in numerous states even though they will have the exact same benefits? What strategies will companies use in developing products to react to the changes brought on by the law?

Due to this upcoming regulatory change, CSG Actuarial expects there will be a gradual shift over the next few years to plans not covering first dollar benefits leading up to 2020 when all new entrants will need to purchase plans not covering first dollar benefits. This shift is taken into account in our projected new annualized premium and total premiums in Table 6.

Conclusion

Data continues to suggest the Medicare Supplement market offers strong opportunities for growth for carriers, marketing organizations, and agents. We expect there will be two primary factors fueling this future growth.

Factor 1 – Overall Medicare Growth

The ongoing growth in the Medicare market from incoming Baby Boomers will increase the number of Medicare beneficiaries by 20 million over the next 11 years. The number of Medicare beneficiaries in 2025 will be 37% higher than it was in 2014 and Medicare Supplement plans will grab their share of this expanded market.

Factor 2 – Decrease in Retiree Health Benefits

Economic issues and accounting changes continue to force many companies and municipalities to eliminate or alter health care benefits for their retirees. Many of these companies are offering their Medicare-aged retirees a monthly stipend to purchase their own individual Medicare Supplement or Medicare Advantage coverage. CSG Actuarial expects this trend to continue in the future with Medicare Supplement companies now creating specialized products to handle the unique risk dynamics of this growing market opportunity.

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