How likely are medical schemes to catch the Covid-19 wave

By Milton Segal

29 Jun 2020

When the clock struck midnight on 31 December 2019, and wishes of health, happiness and prosperity for the new year were extended by all, no one could have imagined the trauma that 2020 would bring only a few weeks later.

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Covid–19 was declared a global pandemic and within a few short weeks, this virus with flu-like symptoms drove almost all countries into a lockdown, forcing the majority of industries to shut down and confine people to the safety of their homes. While one understands, to an extent, the rationale for declaring a shutdown, it is questionable that the short-, medium- and longer term effects of virtually shutting down an economy were and are fully understood. As President Cyril Ramaphosa, said, these are unprecedented times that required almost unprecedented and drastic decisions.

South Africa is gradually moving out of what is reported as one of the longest official lockdown periods globally, now approaching almost 100 days, in essence five times longer than the 21 days as originally announced. Industries have been left devastated with the tourism and leisure, restaurant as well as health and beauty among the hardest hit. One such industry that may just produce results better than expected, or perhaps, better than most of the other insurance type industries, is that of medical schemes.

Credit risk

For most South Africans in formal employ, it is compulsory that they be a member of a private medical scheme unless they are already a dependent on a spouse’s medical scheme, either way then, they are ‘covered’. So significant is this, that in almost all cases of formal employment, the medical aid payment is deducted directly by the employer, as would be similar in the case of PAYE, UIF, etc., and paid over to the medical scheme. This greatly reduces the risk that an employee does not have sufficient funds to cover his/her required monthly medical installment and also eases the risk of non-collection of premium by the medical scheme itself.

When an employee leaves their job they have the option of either continue on the scheme and pay directly or withdrawing from the scheme. As a rule of thumb, if a member misses a payment to the scheme, the membership is terminated or at best suspended unless an arrangement with the scheme is made. Cover for the employee terminates immediately, as does the scheme's financial exposure to the (former) member. Either way, the scheme is protected against 'credit risk'.

For the vast majority of salaried South Africans who have continued to earn a salary during lockdown, or even a partial salary, the employers would have had to continue paying over the employee's contribution to the medical schemes. So from a collection and revenue perspective, revenue from active members are likely to remain close to budget for a medical scheme, even during Covid-19. Fortunately, the number of people who fall gravely ill as a result of contracting Covid–19 and that require admission to hospital, let alone ICU, is very low in % terms, around 4-5%. Again, that bodes well for medical schemes whereby only a very small fraction of their members may require the scheme to pay for expensive hospitalisation. If so, could medical schemes not be caught by the coronavirus in 2020?

Interestingly, either because of the majority of members' reluctance to go for the more routine type medical checkups such as dentistry, physicians, physiotherapy and elective type surgeries in an effort to decrease the risk of exposure, or, because many medical facilities are simply only offering emergency medical treatment to reserve hospitals for ill patients, it is very likely that the majority of medical scheme members have not used as much of their medical aid benefits as would ordinarily have been the case six months into the financial year in a 'normal', non-Covid-19 year.

The schemes then, by way of analogy, would have collected almost all the premiums it should have collected from active members (inactive members pose no financial risks to the scheme) but incurred significantly less expenses than ordinarily the case. With numbers of coronavirus cases continuing to rise at an increasing rate, it can be expected that this trend may continue well into quarter three and perhaps quarter four of 2020. Could this somewhat ironically leave schemes in a financially healthier position than ordinarily would have been expected during this Covid–19 pandemic?

Results

Medical schemes will soon be presenting their interim, six monthly results to the public. It will be of extreme importance that the information be disclosed in a way as to explain the outcomes and fluctuations in results.

The schemes' audit committees, risk and governance committees as well as boards of directors have a fiduciary duty in this regard to protect both the interests of the scheme itself and its members by producing corporate reports that are reliable, accurate and free from material misstatement. Caution will also have to be applied when the schemes start considering the percentage increase in member contributions for 2021 and will need to balance their current reserves, future reserve requirements, medical costs that are certain to rise at an increasing rate in the foreseeable future due to currency weakness and general above inflationary increases. Schemes will also need to factor in the likelihood that they will see an increase in 2021 of the elective type treatments mainly as a result of members either not being able or not willing to do so in 2020.

Detailed notes disclosures, judgements made, assumptions used and forecasted cash flows will be required to produce information that will be understood by both shareholders, investors, and the scheme members themselves. Clear and transparent information will be of the utmost importance as to understand the results and what the remaining six months may bring. There is, perhaps, a danger that the schemes end up producing results that would appear to reflect that the schemes are benefitting financially as a result of the pandemic and escape the financial burden that the majority of both the country's and world's companies are experiencing – a case of medical schemes being immune to the Covid-19 pandemic?

Never before has the importance and reliability of financial and integrated reporting been this important to members, investors, suppliers, regulators and the country itself. Covid-19 is indeed not just a medical pandemic, but a financial one too.

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