

FACT SHEET

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INDUSTRY MEDIA FORUM

POSITION ON THE NATIONAL HEALTH INSURANCE (NHI)

- On Friday 12 August 2011 the Department of Health (DoH) released the National Health Insurance green paper. Mediclinic supports the responsible and pragmatic methodology proposed in the paper and believe a gradual phasing-in period is appropriate for the South African context.
- Mediclinic fully supports the principle of improving access and affordability of healthcare to all South Africans and we would like to participate in the further development of NHI.
- The private hospital sector is a national asset and as such we can contribute positively to the process.
- To realise the vision of increasing access to quality healthcare for the entire population, South Africa will need both the public and private healthcare systems. Mediclinic looks forward to the opportunity of playing a bigger role, specifically through Public Private Partnerships, while the public sector remains the backbone of healthcare services in the country.
- Mediclinic supports a multi-tier healthcare system as the most optimal way to ensure universal access to quality healthcare. We look forward to receiving detail on the proposed funding of NHI – a critical aspect that is yet to be addressed.
- The shortage of healthcare professionals is one of the main problems faced by the private and public sector and a shortage that can only be overcome by working together. We believe that Mediclinic can contribute greatly in this regard.
- Mediclinic is a registered tertiary education institution that runs six learning centres and two satellite campuses where more than 1000 nurse practitioners are trained annually.
- Mediclinic aims to continue its support for training by partnering with government to educate doctors and nurses.

POSITION ON PRICE REFORM

- The image that is often depicted of private hospitals is that they have *disproportional* price negotiating power. It is thus incorrectly argued that this results in excessive price increases and therefore the main reason for real increases in medical scheme contribution rates.
- Mediclinic's Health Policy Unit has embarked on a comprehensive research initiative to contextualise many of the myths and misconceptions related to pricing. The information below provides a summary of the most salient points.
- Mediclinic needs for the DoH and the Council of Medical Schemes (CMS) to take cognisance of the challenges faced by private hospitals, to ensure the long-term sustainability of South Africa's healthcare system as a whole.

- The regulation of the medical scheme industry in terms of the Medical Schemes Act (with enabling regulations that came into effect on 1 January 2000) caused major increases in costs, and therefore the contribution rates of medical schemes.
- Social Health Insurance – a critical component of the Act, that aims to eradicate any discriminatory tendencies towards the old and sick – can only work if the measures to protect the elderly and sick are *balanced by measures to ensure the future stability of the risk pool*.
- The three main measures introduced through the Medical Schemes Act are: open enrolment, community rating, prescribed minimum benefits (PMB's).
- Since 1 January 2000, the DoH and CMS have neglected to introduce the planned reforms required to ensure stability of medical scheme risk pools.
- The fact that the Risk Equalisation Fund (REF) has not yet been implemented means that medical schemes *compete primarily on the basis of attracting young and healthy individuals*. This leads to lower average claiming patterns which allows for more competitive contribution rates and thus stronger membership growth.
- The cost of memberships has risen at a higher level than it would have if the medical schemes had a greater number of younger and healthier members.
- The introduction of the REF *would significantly reduce this incentive to cherry pick the good risk* and would thus lead to greater focus on increasing administrative efficiencies and the management of healthcare utilisation.

MEDICLINIC SUPPORTS REFORM – COST AND PRICING MUST BE UNDERSTOOD

- The policy reform of adjusting the current tax exemption subsidy for medical scheme contributions to a tax credit will greatly increase the income cross-subsidies in the market and thus improve the affordability of private healthcare for low income families.
- Further causes of cost increases resulting from the introduction of the Medical Schemes Act, include the following: solvency requirements; the ever-increasing reporting requirements imposed by the CMS on medical schemes; the implementation of benefit design programmes which put primary healthcare services in a 'savings' component and the lack of active health promotion.
- If there is a greater emphasis on wellness and preventative care, the incidence of preventable serious illnesses and consequently the costs of treatment, would decrease.
- The medical scheme population has not grown at the same rate as the growth in South African population for numerous reasons. The medical scheme main members, as a percentage of the formally employed, has been relatively stable over the ten year period, indicating that the *relatively poor growth of the formal employment*, and not the affordability of medical scheme insurance, was the cause for the slow growth in the number of medical scheme beneficiaries, compared to the population growth over this period.
- Often the decrease in medical schemes is cited as 'proof' of the decline or instability in the market.
- Large risk pools, as opposed to fragmented pools, are more favourable according to the World Health Organisation.
- A large pool can take advantage of economies of scale in administration and reduce the level of the contributions required to protect against uncertain needs, while still ensuring that there are sufficient funds to pay for services.
- In the South African medical scheme environment, each option within a medical scheme is a separate risk pool as legislation requires each option to be financially self-sufficient and self-sustaining. There were 355

separate risk pools or options in South Africa in 2008, of which only 80 were sufficiently large to accept full healthcare risk, using the Milliman USA definition of a minimum of 20 000 lives.

- More consolidation in the medical scheme industry is necessary in order to create larger risk pools to ensure greater efficiency of risk pooling.
- As far as CPI is concerned, the rise in healthcare costs in excess of CPI is not only a South African phenomenon. Research shows that most countries have experienced medical expenditure that outstrips CPI from 2000 to 2007.
- It is also evident that Mediclinic's price increases have been consistently *lower* than nursing salary inflation in the observed period (2002 – 2010).
- Medical scheme expenditure on private hospitals is driven by both utilisation and price.
- Since medical scheme contributions have increased in *excess* of salary inflation, it can therefore be concluded that utilisation and not price is the factor driving up medical scheme contributions, reducing the affordability of medical scheme cover.

HOSPITAL PRICE INFLATION AND RETURN ON INVESTMENT

- Hospital price inflation has been significantly lower than salary inflation, indicating, again, that increased pressure on affordability is driven to a larger extent by increases in utilisation rather than price.
- The often repeated assertion that the prevalence of HIV/AIDS is roughly 1% in the medical scheme market is untrue. The 1% figure is in fact not a reflection of the prevalence of HIV, but the proportion of medical scheme beneficiaries who have registered for HIV disease management programmes.
- The fact that a large proportion of HIV-positive beneficiaries are not registered and is thus not actively being managed for the disease, *leads to a far greater incidence of such beneficiaries being hospitalised with complications*. This further drives up the *utilisation* of healthcare services.
- Our research clearly illustrates that there is a clear change in the *age distribution of patients* – with a move towards relatively fewer patients at younger ages and relatively more at older ages. Due to the kind of procedures that older people are admitted for and the concomitant longer lengths of stay, the average hospital admission for a 70 year old patient is roughly double that of a 25 year old. This phenomenon impacts medical schemes through increased utilisation, not price.
- The increased intensity of care which is due to changes in age distribution, and the anti-selection impact of open enrolment is *driving up utilisation of private hospital services*.
- Utilisation is also driven up by the increasing burden of disease and the introduction and increased use of new technologies.
- The stagnation of funding to public hospitals since 1994 (as alluded to in the Additional Discussion Documents dealing with the proposed NHI scheme presented at an ANC general council in 2010) has had an adverse effect on the quality of care at public hospitals. Since 1988 medical scheme claims paid to public hospitals decreased from 25% to less than 5% – this failure of public hospitals contributed greatly to the extent to which private hospitals experienced increase utilisation of their facilities.
- There is a misconception that the private hospital sector generates very high ('super-normal') profits. However, private hospitals make a justifiable and necessary return on investment.
- Return on investment of the private hospital industry in South Africa over the five years ending in 2007, shows that, measured against the average value of capital employed, the listed private hospital companies' after tax returns were 5.7% which are ***considerably lower than the 13.4% average of the 40 largest JSE-listed companies***. This according to *PricewaterhouseCoopers*.

- The CMS suggests – according to a research methodology that has never been explained or where private hospitals were never given an opportunity to give input – that private hospitals were earning return on investment of close to 25%.
- This is not correct. The return on average capital employed of the top 40 JSE listed companies were 12.4% over the past five years. If the private hospital industry's return were *more than double that* (as suggested by CMS research), it stands to reason that the private sector share prices would have outperformed the JSE average. However, Mediclinic's share price is lagging the JSE performance.

SUSTAINABILITY IS KEY

- The sustainability of the private hospital industry is dependent upon its ability to provide returns on investment sufficient to justify the risks associated with the huge investment of capital which it requires.
- Nurse salaries are a significant input cost to private hospitals making up 50% of private hospital costs
- The advancement of medical technology has also caused a significant increase in the capital related to the building and equipping of a private hospital.
- Figures prove that hospital cost inflation cannot be compared to CPI, since a significant aspect of Mediclinic's cost inflation is driven by nurse salaries and new technology, which are the primary reasons for the increase in real costs.
- Mediclinic believes that the DoH misapprehends the effect of private hospital profits on medical scheme contribution rates.
- Private hospital profits amount to a small proportion of medical schemes' total payments to health service providers and an even smaller portion of medical schemes' gross contribution income.
- Payments to private hospitals make up about 33.0% of medical schemes' gross contribution income of R84.8 billion for 2009. If private hospitals were to reduce prices to the extent that they halve their EBITDA margins (which is completely unsustainable in practice), payments to private hospitals would *decrease* from 33.0% to about 30.6% of medical schemes' gross contribution income.
- If there is a commensurate reduction in medical scheme contribution rates, the average medical scheme beneficiary who paid R890 per month in 2009 (according to the CMS), will pay only R32 less per month, i.e. a reduction of 3.5%.
- Domestic healthcare costs are largely driven by factors such as new technologies and procedures, an ageing population, the increased burden of disease and HIV/Aids, as well as the shortage of skilled staff.
- The largest component of costs tends to be hospital-related, followed by specialists and then medicines.
- Hospitals continue to make concerted efforts to *improve efficiencies and try and absorb costs instead of passing all their costs increases on to consumers*.
- It is estimated that the private hospital industry's inflation rate has been maintained at a relatively low level of 5.6% in 2006, from 5.2% in 2005 (2004: 8.1%). This is according to a Global Credit Rating's report ("South African Medical Scheme Ratings Bulletin" August 2007) that shows South Africa's hospital tariffs are ***not out of control***.
- The "billed methodology" used to calculate occupancy rates allows for half days and is most commonly used in the South African private hospital industry. However, most developed countries use the "census methodology" to calculate occupancy rates, where half days are counted as whole days. The "census methodology" is therefore a better measure when doing international comparisons of occupancy rates.
- Occupancy rates based on the "census methodology" are significantly higher than that calculated on the "billed methodology" as illustrated by our research (pg. 23 of research report).

- Mediclinic's occupancy rates have shown an *increasing* trend over time. Since Mediclinic's EBITDA margins have remained **constant** over this period, this indicates that *higher occupancy rates are used to sustain profit margins at lower tariffs*. In other words – medical schemes and their members have received the benefits of increased scale and efficiency through lower than required hospital tariffs.

FUNDING AND CONTRIBUTIONS

- The public hospital sector is financed through general taxes and every citizen of the country has an entitlement to health care services provided by public hospitals.
- The private hospital sector is primarily financed through medical scheme contributions.
- Those who opt to join medical schemes are those who (after paying their taxes), still prefer to make *additional contributions* to access private health care (especially private hospital services).
- The demand for private hospital care amongst the low-income groups has increased significantly – contributing to the debate around “affordability” within the private hospital sector.
- The misplaced focus on trying to achieve “affordability” within the private sector for all South Africans is due to the lack of understanding that private hospital services are not a merit good.
- Patients in the public sector do not pay for hospital services based on the cost of the service they have consumed, because costs are heavily subsidised by general taxes.
- Contributions to medical schemes (based on the option selected by the beneficiary) are determined by an expected benefit. In addition, out-of-pocket payments are reflective of the cost of providing the service.
- Private hospital services are not merit goods, and therefore prices of hospital services to patients (or intermediaries such as medical schemes) must reflect the cost of delivery of the relevant services.

MORE ABOUT MEDICLINIC

- Mediclinic International is a South Africa-based international private hospital group with three operating platforms in Southern Africa (South Africa and Namibia), Switzerland and the United Arab Emirates.
- The group was founded in 1983 and has been listed on the JSE Limited, the South African stock exchange in Johannesburg, since 1986.
- Mediclinic Southern Africa represents the Southern African operations of Mediclinic International, one of the largest private hospital groups in the world.
- Dr Edwin Hertzog, the current Chairman, commissioned by the then Rembrandt Group (now Remgro Limited) undertook a feasibility study in 1983 on private hospitals which led to the foundation of Mediclinic.
- The group focussed on purchasing and developing flagship medical facilities in Cape Town and Johannesburg from 1984 to 1986.
- From 1995 Mediclinic Southern Africa focussed on acquisitions of the Medicor Group, the Hydromed Group, the Hospiplan Group and the Curamed Group. A period of revitalisation followed with major renovations and upgrades to these properties.
- In 2006 Mediclinic was established as a global hospital group through the acquisition of the controlling interest in Emirates Healthcare, the largest private hospital group in Dubai and Hirslanden, a private hospital group in Switzerland.
- Mediclinic International strives to be the leading international hospital group and the world-class benchmark for acute private healthcare.
- Mediclinic International provides access to the largest community of medical specialists through our 68 hospitals across three continents.

- Today Mediclinic Southern Africa operates 49 hospitals throughout South Africa and three in Namibia with more than 7 000 beds in total.
- Hirslanden operates 14 private acute care facilities in Switzerland with more than 1 400 beds;
- Emirates Healthcare operates two hospitals with 336 beds and eight clinics in Dubai, United Arab Emirates.
- Most specialist disciplines are available at the group's hospitals, which are supported by approximately 23 200 staff members – with Mediclinic Southern Africa employing approximately 16 000, Hirslanden approximately 5 600 and Emirates Healthcare approximately 1 600 employees.
- Mediclinic's commitment to quality care is a key focus area in all the activities throughout the Group. The Group has established a culture of quality that permeates every aspect of the business and its dedication to excellence in healthcare is evidenced by the quality of care and its facilities.
- The Group strives at all times to provide international comparable quality care in an environment that is safe to both patients and staff. Its continued focus on expert care stretches from the skills of supporting doctors to the care of patients, from the empathy of its nursing staff to the high standards of its facilities, from the meticulous maintenance of world-class technology to upholding the fairest possible tariff.
- Mediclinic prides itself on providing an excellent private hospital service where patient care always remains at the centre of its business – well-founded on the science of care, providing expertise that you can trust.