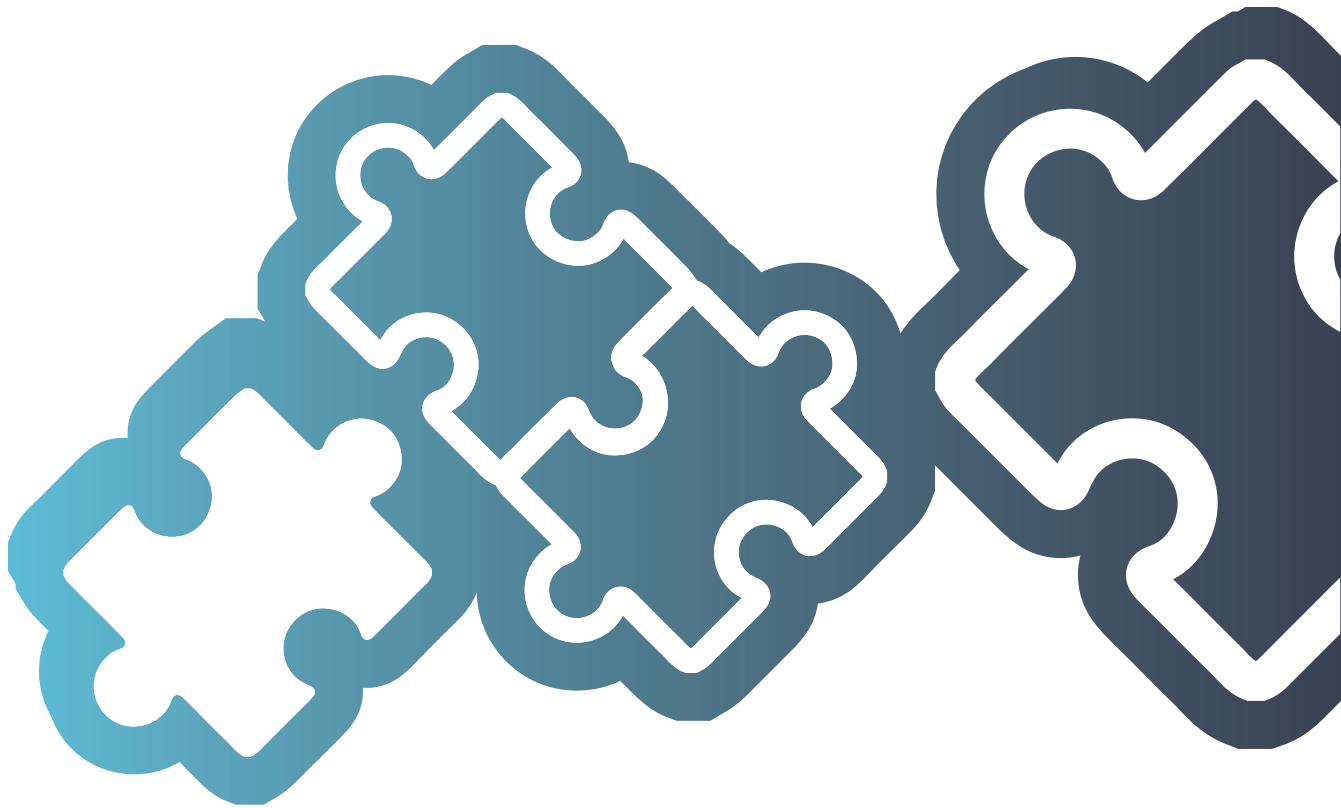


# The Future of Medicare Supplement

## 7th Annual Market Projection

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2017



Jared Strock, FSA, MAAA  
Douglas Feekin, ASA, MAAA

CSG Actuarial

Authors

Jared Stroch, FSA, MAAA  
 Douglas Feekin, ASA, MAAA

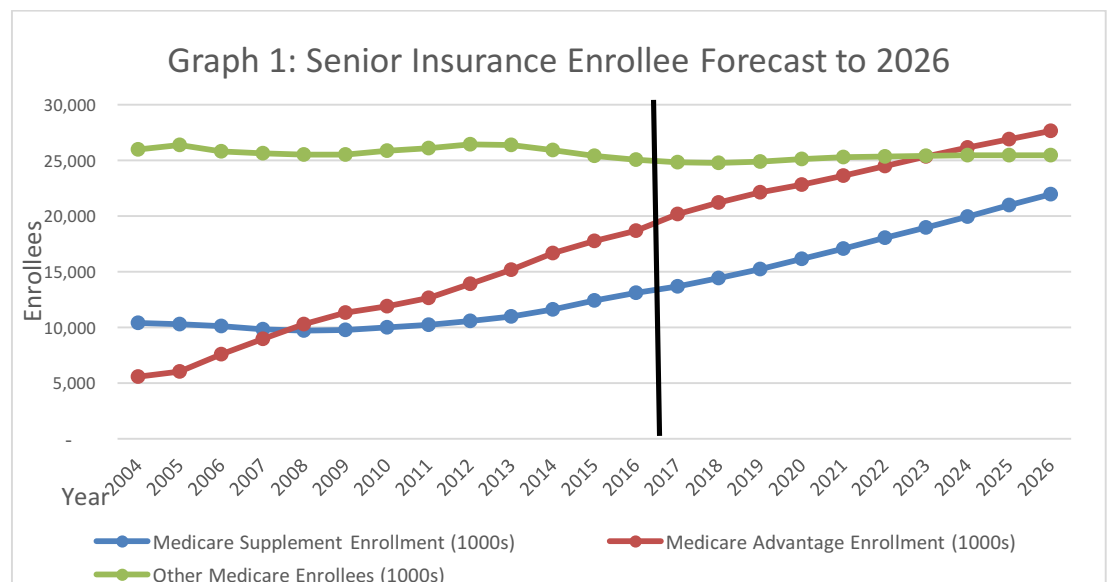
## Introduction

The Medicare Supplement market continues to offer long-term sustainability. Just over 75 million individuals are expected to be enrolled in the Medicare program by 2026 (a 32% increase over 2016). This means that by 2026 roughly 20 million more individuals will be added to the Medicare program with another 10 million being added by 2035 (Table 2).

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).

Sources

1. 2017 Medicare Trustees Report
2. NAIC Medicare Supplement Experience Exhibits
3. CMS.gov
4. Other Public Company Sources
5. CSG Actuarial Projections



## 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 the Medicare Supplement market is expect to grow over the next 10 years, we first evaluated the current Medicare population using the following demographic factors:

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

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

Table 1						
Medicare Beneficiary Data (in 1000s) - 2016						
Category	All Enrollees		Medicare Supplement		Medicare Advantage	
	Number	% Dist	Number	% Dist	Number	% Dist
<b>Total Enrollment</b>	56,800		13,094		18,658	
<b>Eligibility Status</b>						
Aged	47,750	84.1%	12,756	97.4%	16,148	86.5%
Disabled	9,050	15.9%	338	2.6%	2,497	13.4%
<b>Age</b>						
Under 45 Years	1,943	3.4%	70	0.5%	363	1.9%
45-64 Years	7,107	12.5%	268	2.0%	2,134	11.4%
65-74 Years	26,783	47.2%	7,036	53.7%	8,899	47.7%
75-84 Years	14,281	25.1%	4,060	31.0%	5,173	27.7%
85 Years or Older	6,687	11.8%	1,660	12.7%	2,075	11.1%
<b>Gender</b>						
Male	25,829	45.5%	5,532	42.3%	8,092	43.4%
Female	30,971	54.5%	7,562	57.7%	10,566	56.6%
<b>Annual Income</b>						
\$10,000 or Less	6,112	10.8%	351	2.7%	1,905	10.2%
\$10,001-\$20,000	12,860	22.6%	1,950	14.9%	4,890	26.2%
\$20,001-\$30,000	10,167	17.9%	2,412	18.4%	3,985	21.4%
\$30,001-\$40,000	7,140	12.6%	1,976	15.1%	2,480	13.3%
\$40,001-\$50,000	5,521	9.7%	1,644	12.6%	1,642	8.8%
\$50,001 or More	14,995	26.4%	4,761	36.4%	3,756	20.1%
<b>Area of Residence</b>						
Urban	43,827	77.2%	9,230	70.5%	15,934	85.4%
Rural	12,973	22.8%	3,864	29.5%	2,724	14.6%
<b>Health Status</b>						
Excellent	9,571	16.9%	2,653	20.3%	3,168	17.0%
Very Good	16,392	28.9%	4,485	34.3%	5,472	29.3%
Good	15,955	28.1%	3,757	28.7%	5,375	28.8%
Fair	10,235	18.0%	1,600	12.2%	3,286	17.6%
Poor	4,646	8.2%	599	4.6%	1,356	7.3%
<b>Living Arrangement</b>						
Lives Alone	16,268	28.6%	3,938	30.1%	5,480	29.4%
With Spouse	28,996	51.1%	7,548	57.6%	9,211	49.4%
With Children	5,867	10.3%	816	6.2%	2,131	11.4%
With Others	5,663	10.0%	792	6.0%	1,834	9.8%

Sources

1. 2017 Medicare Trustees Report 2013 Medicare Beneficiary Survey
2. NAIC Medicare Supplement Experience Exhibits
3. CMS.gov
4. Other Public Company Sources

Disclaimer

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

### Key Observations from Table 1:

- The Medicare Supplement market has a substantially lower proportion of disabled insureds than the Medicare Advantage market.
- Income distribution among products shows that Medicare Supplement plans typically appeal to insureds with higher annual income on average.
- The proportion of rural insureds who have a Medicare Supplement plan is significantly higher than the proportion of rural insureds who have a Medicare Advantage plan.
- The Medicare Supplement market has a higher proportion of healthier individuals compared to the Medicare Advantage market.
- About 70% of all Medicare Supplement beneficiaries live with someone else. The majority of carriers selling Medicare Supplement today offer some version of the household discount.

### Medicare Eligibility Projection

Table 2 features the overall Medicare beneficiary projection. The growth projected by the 2017 Medicare Trustees Report is being driven by the well documented influx of baby boomers now turning 65 and joining the Medicare program.

Source

1. 2017 Medicare Trustees Report

Table 2			
Year	Total Medicare Beneficiaries (1000s)	% Increase By Year	
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	52,504	3.2%	
2014	54,115	3.1%	
2015	55,542	2.6%	
2016	56,800	2.3%	
2017	58,625	3.2%	
2018	60,337	2.9%	
2019	62,178	3.1%	
2020	64,060	3.0%	
2021	65,937	2.9%	
2022	67,832	2.9%	
2023	69,683	2.7%	
2024	71,482	2.6%	
2025	73,305	2.6%	
2026	75,075	2.4%	
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2035	86,178	1.5%	

## Historical Medicare Supplement Assessment

To project the future of the Medicare Supplement market, we started by evaluating historical trends. Table 3 indicates Medicare Supplement policies in-force and premiums have rebounded the past nine years, fueled by an increase in annualized new premiums, which are up 91% since 2008. The increase in annualized new business premiums resulted in a leveling of the Medicare Supplement market penetration percentage from 2009-2013, followed by an increase in each year thereafter. In fact, the percentage of Medicare Beneficiaries who own a Medicare Supplement product increased 0.9 percent from 2014 to 2015, followed 0.8 percent from 2015 to 2016.

### Sources

1. NIAC Medicare Supplement Experience Exhibits
2. 2017 Medicare Trustees Report
3. Other Public Company Sources

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	21.4%	3,600,000
2015*	12,372	27,334,334	2,209	22.3%	3,900,000
2016	13,094	29,039,669	2,218	23.1%	4,200,000

\*2015 numbers were updated from last year's report due to updated data files

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

1. **The number of Medicare beneficiaries has grown by about 25% since 2008** (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 eight 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). The 2016 Medicare Advantage growth rate of 5.1% is the lowest growth rate since 2010.
3. **Employers have continued to remove Medicare-aged retirees from their employer health plans**, with some providing them with a stipend to purchase individual coverage. Due to this, the percentage of Medicare beneficiaries not in Medicare Advantage or Medicare Supplement plans has declined dramatically

the past 10 years (“Other” column in Table 5 & “Other Medicare Enrollees” in Graph 1).

As a result, the annual growth rate of Medicare Supplement beneficiaries has been at its highest rate in recent years coming in at 6.9% in 2015, followed by 5.8% in 2016 (Table 4). At the same time, the Medicare Advantage annual growth rate of beneficiaries dropped to 6.8% in 2015, followed by 5.1% in 2016, bringing the growth rate of Medicare Supplement and Medicare Advantage closer than it’s ever been.

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%	7.8%	10,199	2.4%	2.1%
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%	
2015	17,761	6.8%	7.7%	12,372	6.9%	5.6%
2016	18,658	5.1%		13,094	5.8%	

Sources

1. NIAC Medicare Supplement Experience Exhibits
2. CMS.gov

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	52,504	26,133	26,371	50.2%
2014	54,115	28,204	25,911	47.9%
2015	55,542	30,133	25,409	45.7%
2016	56,800	31,752	25,048	44.1%

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.
- 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. The projection assumes average premiums will be level until dropping in 2020.
- 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.

Sources

1. 2017 Medicare Trustees Report
2. NAIC Medicare Supplement Experience Exhibits
3. CMS.gov
4. Other Public Company Sources

Year	Total Policies Inforce (End of Year)	Total Earned 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	21.4%	3,600,000
2015	12,372	27,334,334	2,209	22.3%	3,900,000
2016	13,094	29,039,669	2,218	23.1%	4,200,000
2017	13,666	30,424,698	2,226	23.3%	4,400,000
2018	14,382	32,140,055	2,235	23.8%	4,700,000
2019	15,201	34,100,134	2,243	24.4%	4,900,000
2020	16,137	36,300,596	2,250	25.2%	5,100,000
2021	17,078	38,564,441	2,258	25.9%	5,400,000
2022	18,008	40,818,619	2,267	26.5%	5,800,000
2023	18,956	43,131,223	2,275	27.2%	6,100,000
2024	19,927	45,513,713	2,284	27.9%	6,400,000
2025	20,942	48,014,219	2,293	28.6%	6,800,000
2026	21,972	50,566,196	2,301	29.3%	7,100,000

Sources

1. 2017 Medicare Trustees Report
2. NAIC Medicare Supplement Experience Exhibits
3. Other Public Company Sources
4. CSG Actuarial Projections

## Prior Projection Comparisons

In last year's version of the Medicare Supplement Market Projection, CSG projected 13,000,000 policies to be in force at the end of 2016, and the 2016 Earned Premium was projected to be \$28,713,682,000, in line with actual results (Table 6).

## Current Market Activity and Possible Impacts to Future Medicare Supplement Consolidation

As of last year's report, Aetna's proposed acquisition of Humana, and Anthem's proposed acquisition of CIGNA were both getting increased regulatory scrutiny, with the U.S. Justice Department suing to block the acquisition attempts citing concerns that the mergers would increase health-care costs and simultaneously reduce choice for consumers.

Since that time, Aetna's proposed acquisition of Humana, and Anthem's proposed acquisition of CIGNA have both been called off.

**CSG Actuarial does not believe any potential merger consolidation will negatively impact the growth in the market. Based on our market perspective, at least 10 new carriers have entered or are in the process of entering the Medicare Supplement market in the last two years. We expect there will continue to be new carriers entering the market based on the favorable demographics, cost effective TPA solutions, sophisticated distribution options and reinsurers actively looking for new partnership opportunities.**

## Cost Sharing Plans and First Dollar Coverage

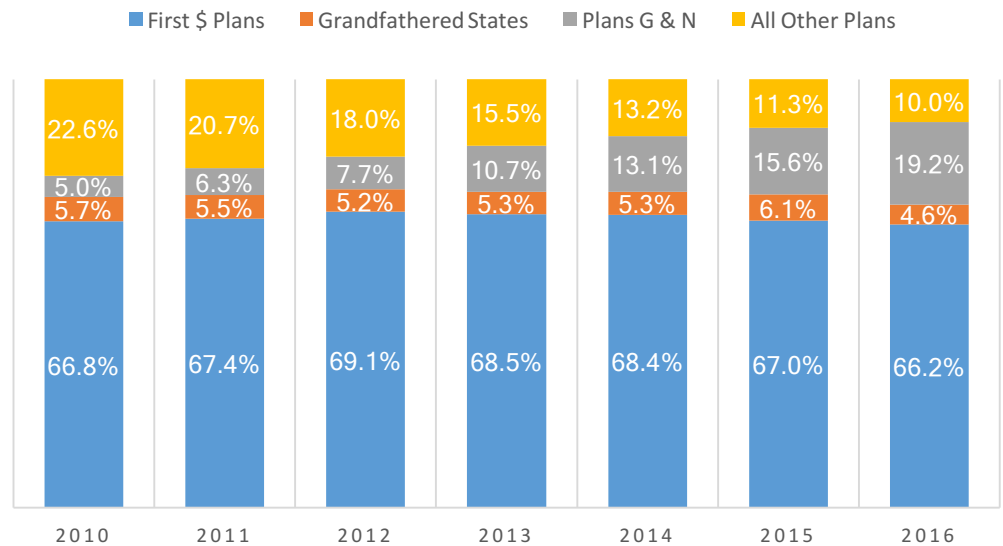
As commonly reported, Plans G and N continue to grow and grab market share in the overall Medicare Supplement market. In 2016, Plans G and N made up over 19% of the lives in the Medicare Supplement market, up from only 5% in 2010. A large portion of the growth in market share for Plans G and N is at the expense of non "first dollar coverage" plans, as can be seen in Graph 2.

Using data from the NAIC, CSG Actuarial grouped the Medicare Supplement lives for 2010 to 2016 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



**GRAPH 2 - MEDICARE SUPPLEMENT DISTRIBUTION OF POLICIES BY PLAN**

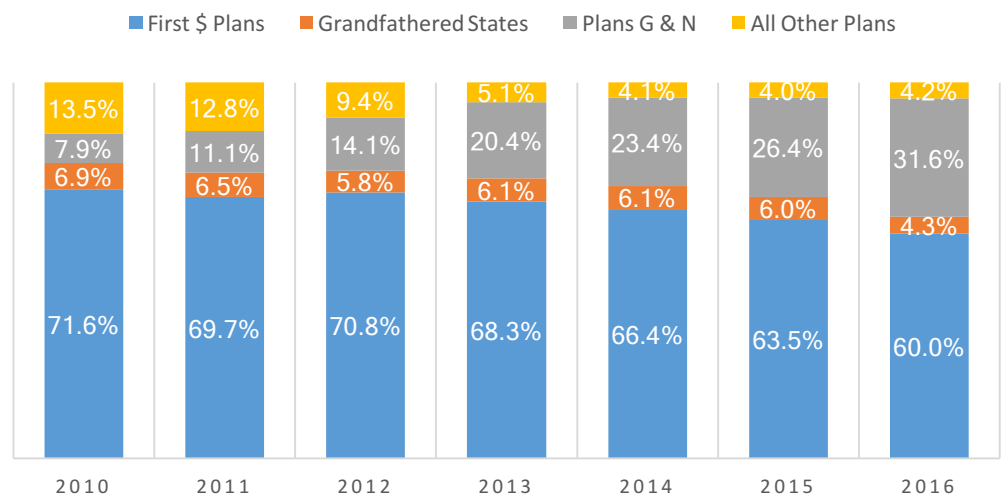


Source

1. NAIC Medicare Supplement Experience Exhibits

This shift to Plans G and N is more obvious when looking at recent Medicare Supplement issued policies. Graph 3 below displays the same information as Graph 2, but is only including the prior 3 issue years for each experience year. In 2016, Plans G and N made up over 31% of the lives issued between 2014 and 2016 compared to 8% in 2010 (for lives issued between 2008 and 2010), while first dollar coverage plans have gone from 72% in 2010 to 60% in 2016.

**GRAPH 3 - MEDICARE SUPPLEMENT DISTRIBUTION OF POLICIES BY PLAN (3 YEARS)**



Source

1. NAIC Medicare Supplement Experience Exhibits

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.

The revisions to the model regulation were adopted by the NAIC in 2016, and the NAIC is recommending that states adopt the updates to the model regulation by 12/31/2017. Some of the details related to the updated model regulation are as follows:

- Plan F can still be sold after 2020 to individuals who were eligible prior to 2020,
- prior eligibles can keep their existing policies (even those that include the Part B deductible)
- newly eligibles will be able to elect Plans D and G in guarantee issue situations,
- carriers will be able to offer a high deductible Plan G starting in 2020.

**Due to this upcoming regulatory change, CSG Actuarial expects there will continue to 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. Carriers, agents, and marketing organizations will need to be strategic with how they price, market and sell products leading up to 2020 and then starting in 2020.**

## Conclusions

Recent results and future projections continue to suggest the Medicare Supplement market offers very strong opportunities for growth for carriers, marketing organizations, and agents. As covered in detail in this paper, some of the primary drivers of this future growth and opportunity will be 1) the overall growth in Medicare, 2) a decrease in Retiree Health Benefits, and 3) slowed growth in the Medicare Advantage program when compared to early years of Medicare Advantage.

As the number of Medicare Beneficiaries continues to grow, from 57 million in 2016 to 75 million in 2026 (table 2), it is becoming clear that those same individuals will increasingly turn to private insurance (both Medicare Advantage and Medicare Supplement) to help cover their insurance needs. While some individuals will continue to receive Retiree Health Benefits, get coverage through Medicaid, or choose Traditional Medicare Coverage without any sort of supplemental coverage (these combined are labeled “Other Medicare Enrollees” in Chart 1 and labeled “Other” in Table 5), these individuals will increasingly make up a smaller and smaller proportion of the total Medicare Beneficiaries.

Beyond those primary drivers, CSG Actuarial believes other factors such as overall market stability and low barriers to market entry will also contribute to the future growth in the Medicare Supplement market. Stability in the market in recent years has been driven by lower claim trends that have led to lower annual premium rate increases and higher company profits. Low barriers to entry in the Medicare Supplement market are a result of numerous experienced TPAs, distributors and re-insurers available to provide

support as needed for new companies wishing to enter the Medicare Supplement market. Adding it all up, CSG Actuarial believes future growth trends within the Medicare Supplement market continue to be very positive.

CSG Actuarial, LLC | 11011 Q St. #101B | Omaha, NE 68137  
(855) 861-8776 | [www.csgactuarial.com](http://www.csgactuarial.com)