

Securing Sustainable Access to Medical and Health Insurance/ Takaful Protection

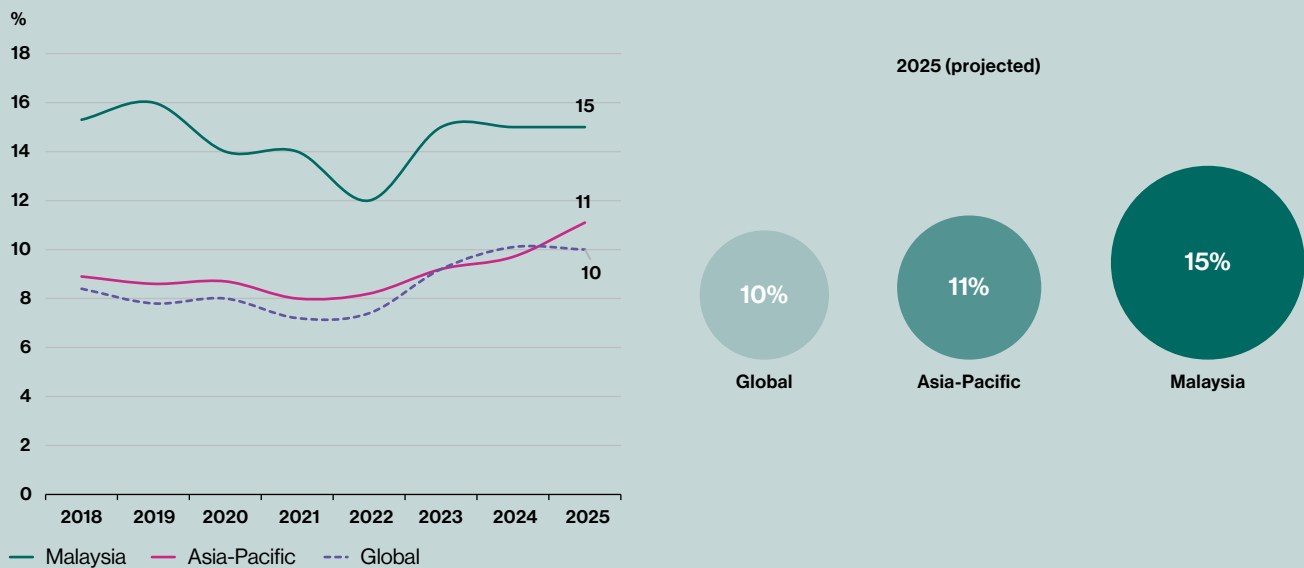
Introduction

As Malaysians age and face higher rates of chronic diseases,¹ healthcare spending is expected to rise. To prepare for unexpected expenses, more Malaysians have begun to purchase medical and health insurance/takaful (MHIT). As of 2023, there are 7.7 million individuals covered under MHIT. Overall, Malaysia spent RM84.2 billion² on healthcare in 2023. Of this, the amount funded by MHIT has grown six times over the past two decades from RM0.96 billion in 2003 to RM6.75 billion in 2023. In this article, we will explore the implications of medical inflation to MHIT premiums,³ strategies to manage medical inflation and secure sustainable access to MHIT.

Medical inflation and its implication to MHIT premiums

Malaysia experiences double-digit medical inflation, which is higher than global and Asia-Pacific averages (Chart 1). Among the factors that contributed to the high medical inflation in Malaysia are the rise of non-communicable diseases (NCDs), ageing population, increase in manpower cost in the healthcare sector and advancements in medical technology. This development has resulted in higher claims payout by insurers and takaful operators (ITOs). To preserve the long-term sustainability of MHIT protection, ITOs will periodically review and adjust the pricing of their MHIT products to ensure that the premiums collected are sufficient to cover the cost of claims made by policyholders.

Chart 1: Medical Inflation in Malaysia vs Regional and Global Average



Source: AON Global Medical Trend Rates Report

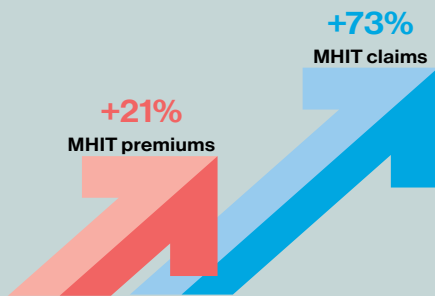
¹ Findings from National Health and Morbidity Survey 2023 show that 15.6% of Malaysian adults have diabetes, 29.2% have hypertension and 33.3% have high cholesterol.

² Includes total expenditure paid by Ministry of Health (MOH), out-of-pocket expenditure by households, MHIT, other ministries, agencies and local authorities, private corporations and non-profit institutions. The expenses include cost of curative, rehabilitative, and long-term nursing care, health promotion and prevention, medical goods and health programme administration. Source: Malaysia National Health Accounts: Health Expenditure Report, MOH.

³ Any reference to insurance policy/insurance premiums/policyholders includes takaful certificate/takaful contributions/takaful participants for standalone MHIT products and cost of insurance (COI)/*tabarru'* for unit-deducting MHIT riders.

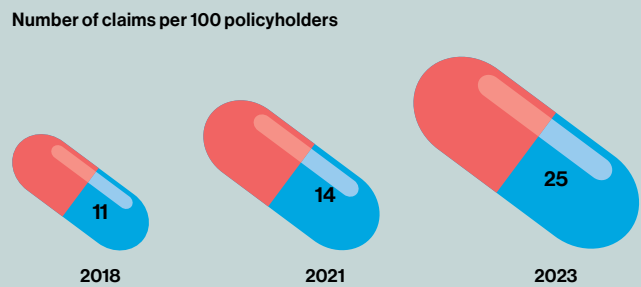
Between 2021 and 2023, the total cost of MHIT claims increased by 73%, far surpassing the 21% growth in MHIT premiums collected (Chart 2). Apart from higher average costs of treatments, this was also driven by more frequent utilisation of medical services as seen by the increase in claims frequency. In 2018, 11 claims were made for every 100 policyholders but by 2023, this number more than doubled to 25 claims (Chart 3). This issue is further compounded by high costs of hospital supplies and services (HSS) such as drugs, laboratory fees and consumables (e.g. gloves). These costs are currently unregulated and show wide variation across hospitals. Given that the HSS component constitutes 59% to 70% of overall private hospital bills, depending on the type of treatment (i.e. non-surgical vs surgical), its impact on overall claims costs is significant.

Chart 2: Trend of MHIT Premiums and Claims, 2021–23



Source: Bank Negara Malaysia and Insurance Services Malaysia

Chart 3: MHIT Claims Frequency, 2018–23



Source: Bank Negara Malaysia and Insurance Services Malaysia

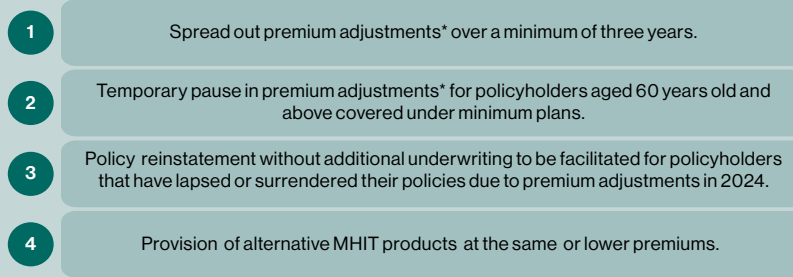
The design of MHIT products also plays a role in this issue. MHIT products with high utilisation limits such as up to RM8 million annually and without lifetime limits, are generally associated with higher healthcare utilisation. Additionally, difference in total charges have been observed for the treatment of similar medical condition between policyholders who receive treatment via cashless facilities, where ITOs issue guarantee letters and make direct payment to medical providers, and those who first make payments out-of-pocket and then seek reimbursement from ITOs.

The persistent rise in claims costs driven by increase in average costs of medical treatments and utilisation of healthcare services over the years, has led ITOs to review the existing levels of premiums and adjust premiums to better reflect expectations of future claims costs. Although such adjustments are a normal practice for ITOs, premium adjustments in Malaysia were more significant in the post-COVID-19 period partly due to the inclusion of adjustments that were deferred by ITOs during the pandemic in 2020 to relieve policyholders at the time. Additionally, medical claims also increased post-pandemic following the resumption of medical treatments and procedures that were earlier delayed and a rise in infectious diseases. In 2024, some of the premium adjustments were quite significant. While 61% of affected policies experienced less than 20% premium increase, about 9% of affected policies experienced more than 40% premium increase.

To alleviate the immediate impact of premium adjustments to policyholders, Bank Negara Malaysia (BNM) in December 2024 introduced a number of interim measures⁴ (Diagram 1). These are temporary in nature to allow some time for the implementation of critical broader health reforms to contain medical inflation. The interim measures cannot be sustained if high medical inflation persists. It is therefore imperative that key stakeholders must holistically and effectively implement broader health reforms to address medical inflation which will be further elaborated in the section titled 'Expediting reforms to effectively address medical inflation' of this article.

⁴ Source: <https://www.bnm.gov.my/-/mhiti-pr>

Diagram 1: Interim Measures for Premium Adjustments in 2024–26



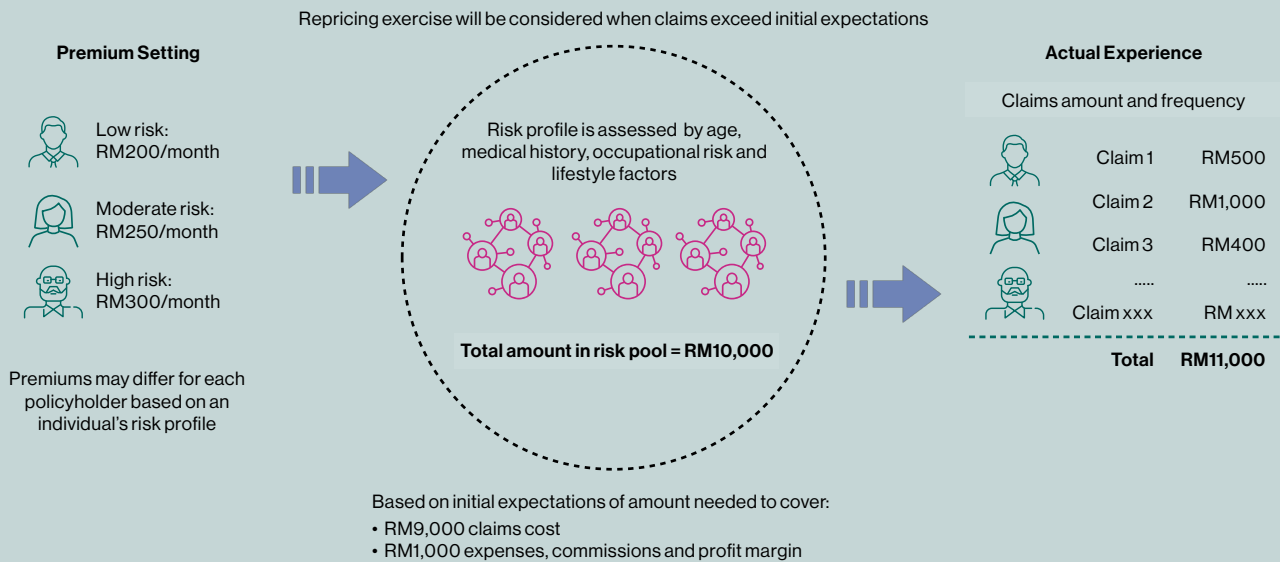
* Applicable to premium adjustments due to medical inflation only.

Source: Bank Negara Malaysia

Premium adjustments depend on the claims experience of risk pools and how often an ITO undertakes a repricing exercise

MHIT products are designed based on the principle of pooling risks between different individuals to distribute the cost of claims and reduce the financial burden of each individual (Diagram 2). MHIT products that provide reimbursement of medical expenses are generally designed with non-guaranteed premiums that are subject to periodic premium adjustments. Hence, the premiums are set with some allowance for inflation until the next expected pricing review period. If the medical inflation experienced by the pool is higher than expected, the future premiums paid by policyholders would have to be adjusted to reflect this in order to ensure that the pool has enough resources to meet claims. This will affect all policyholders in the pool, even if a policyholder has not made a claim or has just entered the pool.

Diagram 2: Risk Pooling

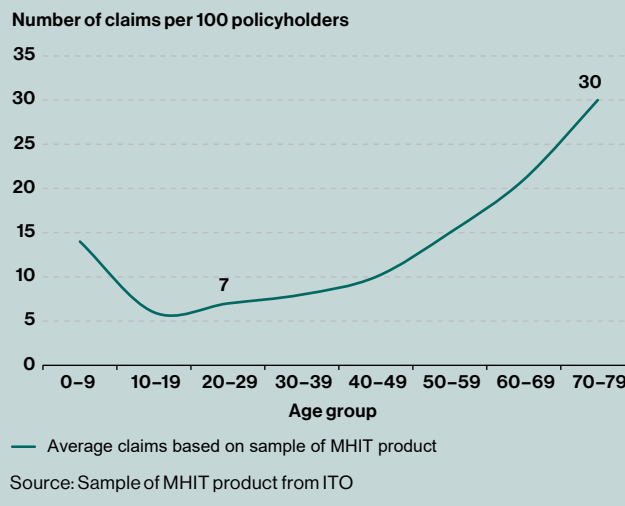


Source: Bank Negara Malaysia

The characteristics of the risk pool will affect the premiums that policyholders pay over their coverage period. Within a risk pool, premiums may vary between individuals based on factors that could affect overall claims on the pool, such as age, gender, medical history, occupational risk, lifestyle factors and plan type. A common factor used to determine MHIT premiums is age. Generally, premiums increase with age, in line with increasing health risks and likelihood of seeking medical treatment. For example, data from a sampled product shows that there are 30 claims for every 100 policyholders aged 70–79 years old. This is significantly higher as compared to seven claims per 100 policyholders aged 20–29 years old (Chart 4).

Differentiated premiums help to achieve a fairer distribution of financial contributions to the pool, in line with an individual's risk profile. On the other hand, it can lead to affordability and access issues for older policyholders including retirees at a time when they have a greater need for protection. Community-rated models where everyone pays the same premium regardless of age and other risk factors is an alternative to the current risk-rating model adopted by ITOs in Malaysia. However, without sufficient scale, appropriate incentives and public policy interventions (e.g. mandatory participation), it can lead to other problems such as adverse selection, low innovation and unsustainable premiums.

Chart 4: Average Claims by Age Group



The size of the risk pool also influences the premium levels during the coverage period. Larger risk pools mean ITOs can spread the financial risk among more policyholders. A large base of policyholders also usually offers a more balanced mix of low-risk and high-risk individuals in the risk pool. This balance helps to keep costs manageable and premiums stable over a longer period. Policyholders in smaller pools are likely to experience greater volatility in claims experience. Recognising the risks of small and shrinking risk pools, BNM allows ITOs to increase risk diversification within a risk pool (e.g. by combining homogenous cohorts) to ensure more stable claims experience within the risk pool going forward.

Premium adjustments are also affected by the frequency⁵ of repricing exercises. ITOs typically conduct repricing every one to three years. Less frequent reviews and a longer interval between repricing exercises may result in a higher premium increase, as the premium adjustments will have to take into consideration expected future medical inflation for a longer period of time.

⁵ For further information, refer to feature article on 'Evaluating the Impact of Medical Re-pricing Deferrals on Life Insurers and Family Takaful Operators', Financial Stability Review – First Half 2021 https://www.bnm.gov.my/documents/20124/4782528/fsr2021h1_en_wb4_medical.pdf.

Features of Investment-Linked Products

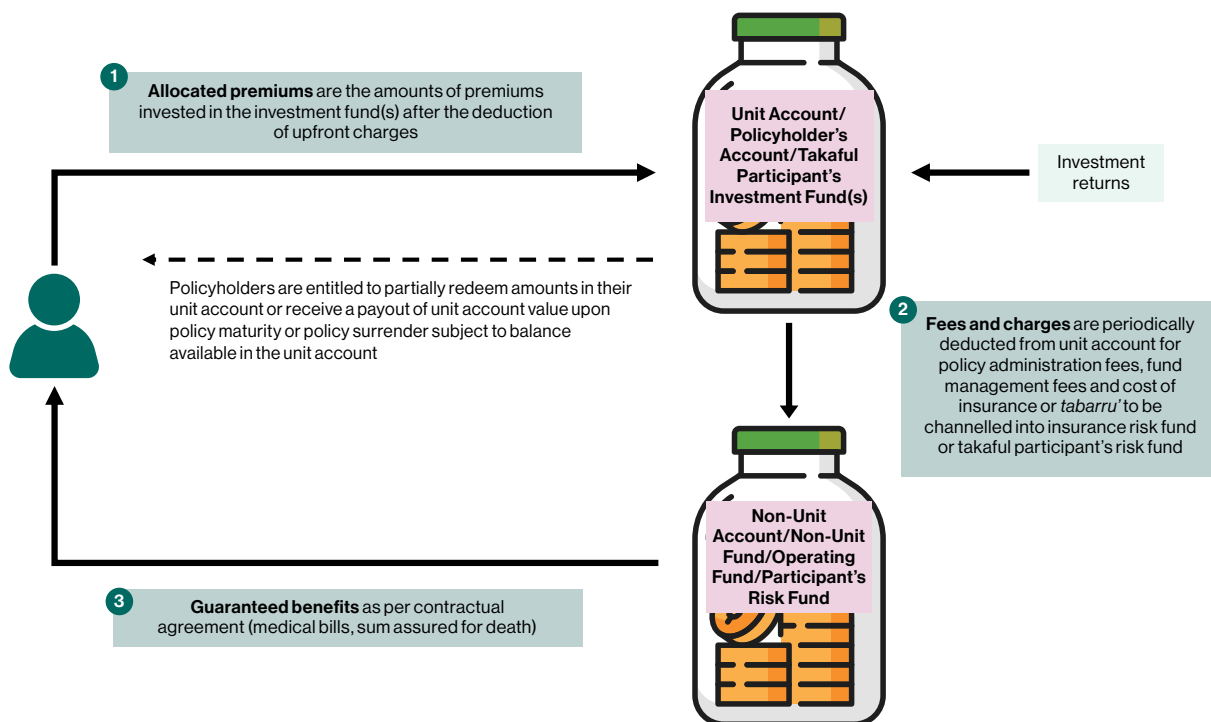
Investment-linked products (ILP) are generally designed with level premiums throughout the policy term. Level premiums mean that the policyholder pays the same premium throughout their coverage period. Level premiums will not go up because of age. However, level premiums can still change (i.e. due to medical inflation) as explained earlier in the article. The premiums, after deduction of upfront charges, will be invested into the investment fund(s) selected by the policyholder. Subsequently, the cost of insurance (COI) and other fees such as fund management fees will be deducted from the policyholder's unit (or investment) account periodically.

The level premiums, plus any investment returns earned, allow the policyholder to grow their unit account from the early years when COI is relatively low. The balance in the unit account is accumulated to cover future increases in COI. However, if medical inflation exceeds initial expectations, the COI is revised upwards, requiring a higher level of premiums to be paid to maintain the level of coverage, similar to other types of MHIT products.

Given this structure, the sufficiency of the unit account to sustain future COI could be impacted by the following reasons:

- a) **lower than expected cash inflow** arising from unfavorable investment returns, policyholder missing premium payments or policyholder does not pay new level of premiums following premium adjustment; or
- b) **higher than expected cash outflow** due to partial withdrawal from the unit fund by the policyholder and increase in COI arising from medical inflation or when policyholder increases coverage without premium top-up.

Diagram 3: Investment-Linked Product



Source: Bank Negara Malaysia

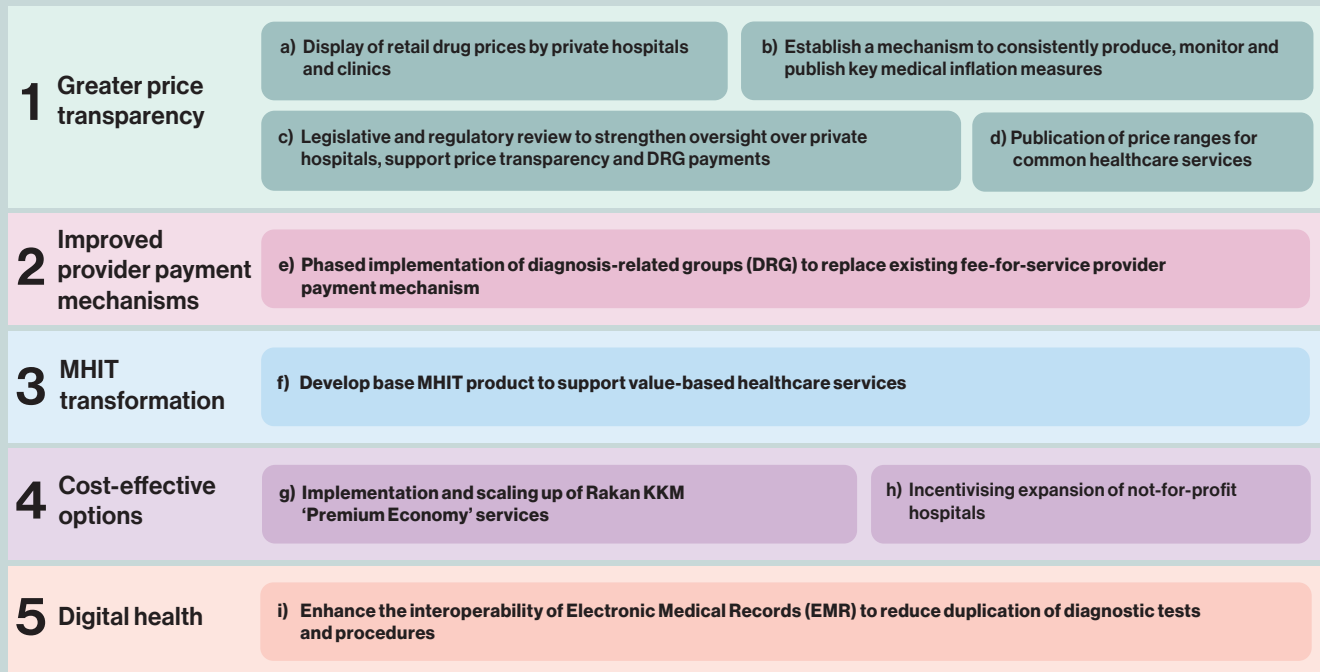
To improve transparency to policyholders, BNM requires⁶ ITOs to disclose the sustainability of policyholders' ILP policies on an annual basis. Key information required in the disclosure includes investment performance and whether the current level of premiums is sufficient to ensure coverage until the end of the policy coverage period.

⁶ Source: <https://www.bnm.gov.my/documents/20124/948107/PD-Investment-Linked-Business-2023.pdf>

Expediting reforms to effectively address medical inflation

Ensuring MHIT remains accessible over the longer term requires addressing the root causes of rising medical inflation. This is important to ensure MHIT products remain sustainable, and policyholders can continue to access the required healthcare services to avoid further burdening the public healthcare system. To this end, BNM together with key stakeholders including the Ministry of Finance, the Ministry of Health (MOH), ITOs, private hospitals and clinics, and consumer groups are working closely to implement nine key initiatives to reduce the pace of medical inflation, guided by five strategic thrusts (Diagram 4).

Diagram 4: Five Strategic Thrusts and Nine Initiatives to Address Medical Inflation



Source: Bank Negara Malaysia and Ministry of Health

The first strategic thrust is to facilitate **greater price transparency**. Initiatives under this pillar include the display of retail prices for drugs and the publication of price ranges for common healthcare services. This publication enables policyholders and ITOs to compare prices across different medical providers while promoting healthy competition. Additionally, a mechanism to consistently produce, monitor and publish key medical inflation measures will be developed, including to better align the methodology with how general inflation is calculated. To support the initiatives, MOH will also undertake regulatory and legislative review of current oversight arrangements of private hospitals.

The second strategic thrust is the implementation of **Diagnosis-Related Groups (DRG) payment mechanism** to replace the existing fee-for-service provider payment mechanism at hospitals. Under DRG, patients are categorised into groups based on their diagnoses and medical needs, adjusting for severity and co-morbidities. Each group is then associated with a predetermined payment amount. This incentivises efficiency and health outcomes, while providing greater price predictability.

The third strategic thrust is **transforming MHIT offerings** via development of a base MHIT product. The development of a base MHIT product aims to deliver a scalable solution that can ensure more sustainable premiums over the long-term through larger risk pooling. The development of the base product will be accompanied by appropriate cost containment measures. Such measures include the implementation of DRG, prioritisation of a cost-effective benefits package and strategic purchasing of healthcare services.

The fourth strategic thrust is increasing the supply of **affordable, mid-tier hospital beds** via the implementation and scaling up of the Rakan KKM⁷ initiative by MOH (which can also serve as a price benchmark) and by incentivising the expansion of not-for-profit hospitals. This initiative will offer more cost-effective options to policyholders.

The fifth strategic thrust is to enhance the interoperability of **electronic medical records (EMR)** across hospitals. EMR will address the current fragmentation of health records in different healthcare facilities. Greater accessibility and portability of a patient's medical data will improve quality and continuity of care while reducing duplication of diagnostic tests and procedures. Over the longer term, this will increase operational efficiency and reduce costs.

The implementation of the five strategic thrusts is expected to reduce the pace of medical inflation and result in cost savings, while ensuring access to quality healthcare in line with global best practices. This will help to contribute to more sustainable premium adjustments over the longer term and secure continued access to MHIT protection. Both the Ministry of Health and Ministry of Finance are supportive of these initiatives and concerted action from all stakeholders across the healthcare ecosystem is key towards successful implementation of the five strategic thrusts.

⁷ Rakan KKM offers 'premium economy' services at selected public hospitals for elective outpatient, daycare and inpatient services. For further information refer to: <https://rakankkm.moh.gov.my/en/>