

***Insurance Times*: S&P: Passing along costs improving insurers' earnings**

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NEW YORK — The ability to transmit higher medical costs to consumers makes for a buoyant near-term earnings picture among U.S. health insurers, according to Standard & Poor's midyear report on the sector.

In the chain of cost increases from hospitals to insurers, from insurers to employers, and from employers to employees, none is proving a weak link.

"Consumers are taking it on the chin," said credit analyst Joe Marinucci. "We're going to see a trend of employees taking on more of the costs and contributing an increasing percentage of premium."

Although consolidation among hospitals has beefed up their negotiating leverage, in terms of the reimbursement rates they can command, insurers have been able to compensate with three years of percentage premium-rate increases in the double digits.

"Employer resistance has been fairly mild," said Shellie Stoddard, a director at S&P's.

Analysts point to the 25% average increase in premiums that the California Public Employees' Retirement System (Calpers) intends to pay as a testament to the industry's bolstered price discipline.

The report praises the current focus on profits rather than revenue and describes health coverage as "the one insurance sector in the U.S. that has exhibited commendable pricing discipline in recent years."

Once employers have accepted higher premiums, employees are bearing the brunt of them, the report notes. Chastened by the experience of restricted access during the reign of HMO coverage in the mid- to late 1990s, consumers are now willing to foot the bill for greater selection in choice of treatments, hospitals, and doctors. It is a trend facilitated by the growing tide of "consumerism", where workers share in the costs of coverage and participate more in their health care buying decisions.

Strong operating results are also assisted by reduced competition in the industry following a spate of consolidation activity since the mid-1990s, particularly among members of the Blue Cross and Blue Shield Association.

The Blue plans are proving increasingly assertive at the national level through the BlueCard program, whereby they can share provider networks and a common claims processing system. Further consolidation among Blue plans is now meeting with political and regulatory resistance, but they remain dominant on home turf.

S&P analysts nevertheless expect the consumer eventually to throw in the towel on price increases.

"In the end something's got to give," said Stoddard. "People are comparing the cost of coverage to mortgage payments at this point."

Policyholder withdrawals from coverage, along with pressures on smaller insurers to fulfill a social mission, could have a dampening effect in the longer term. Meanwhile, costs will keep rising from the provider end as hospitals combine, technological advances multiply, and the population ages.