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Keys to success: Right strategies and partners

Winning in China's health insurance sector

The health industry is one of the most regulated and complex ecosystems in mainland China. While high levels of regulation limits competition from new entrants and product substitutions, none of the players in the ecosystem are operating within developed market conditions. Insurers and to some extent, pharmaceutical companies, are driving the maturity of the Chinese health ecosystem. Multinational insurance companies (MNCs) and new local entrants wishing to enter this challenging yet attractive market, must "find their niches" by formulating the appropriate market entry strategies while collaborating with the right local partners.

China's health insurance sector, which is traditionally dominated by large domestic insurers, is currently experiencing gradual deregulation. However, the value chain integration remains a significant challenge. In order to effectively manage the health care ecosystem in China, finding alternative business models along the "insurance aftermarket" – care management, care provision, care product distribution and care product production – is the potential white space that sub-scale players, such as MNCs and new local entrants, can position their strategic directions to break market-entry barriers.

In terms of the maturity or sophistication level of the industry, greater product differentiation in the private health insurance sector is expected in the next few years, while health insurance products will also move from critical illness to reimbursement, an area that is still underdeveloped in China today. A potential opportunity for MNCs and new local entrants is to partner with local pharma suppliers to jointly establish a reimbursement model that takes value, shared savings and risk into account.

Both parties could also join forces to obtain consumer data needed for condition-specific insurance products, and effectively use analytics and technology to derive insights from the data. This will become the next market trend to help MNCs and new local entrants in China improve their pricing and product design management, in addition to providing better customer experience through digital channels. On the other hand, leading local Chinese insurers are now studying a new way of collecting patient data from the increasing association they have with major public hospitals, following deregulation initiated by local regulators in recent years.

Analytics, which refers to the systematic use of technologies, methods and data to derive insights and enable fact-based decision-making for planning, management, operations, measurements, and learning, can help healthcare organizations measure their performance across cost and quality measurers; understand which clinical processes, physicians, health conditions, and consumers to focus their efforts on; and improve health outcomes. According to the Deloitte Center for Health Solutions 2017 US Health Plan Analytics Survey, analytics is viewed as a major component in an effective population health-management system[1].

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The survey also found that collaborating on analytics can include sharing data inputs, leveraging analytics and incorporating actionable reporting that enables real-time outputs. In our experience, shared analytics strategies between health insurance plans and health systems hold the key to improving quality, reducing cost, and succeeding in the new value-based care environment of the future.

Further studies have discovered that expertise in analytics and a strong data infrastructure are crucial to advanced customer segmentation as well. This expertise, meanwhile, can help with traditional applications, which use consumer research to make customer interactions more straightforward and enable highly innovative applications.

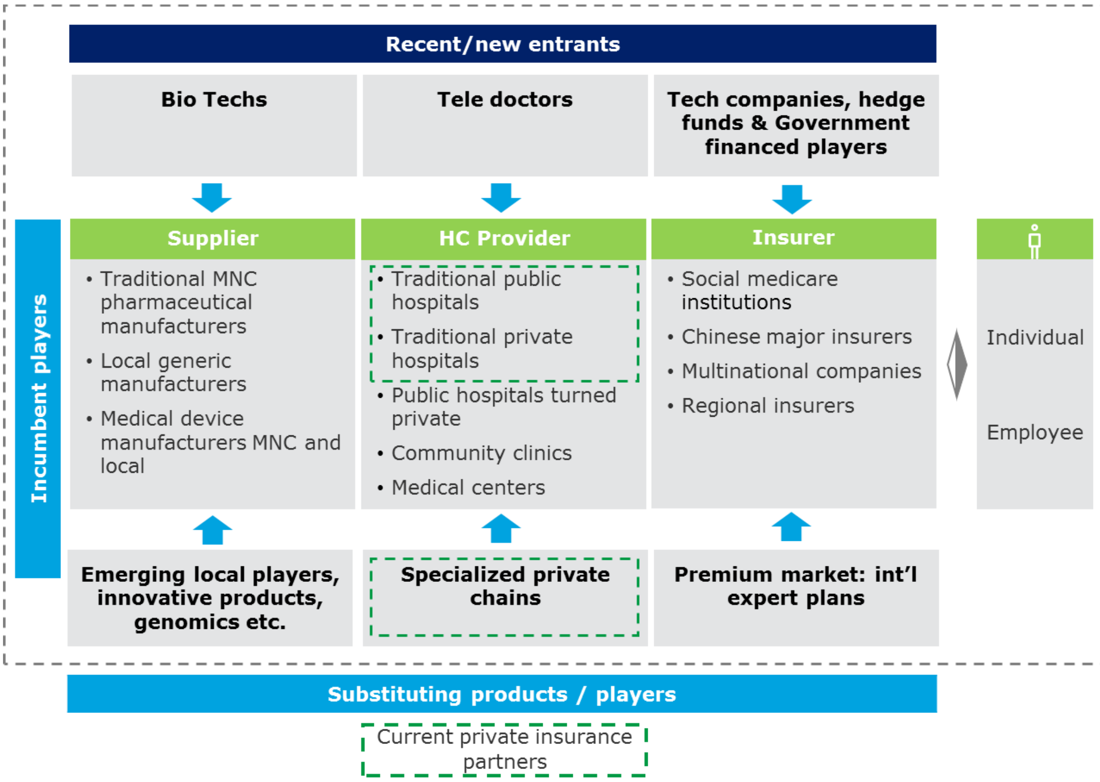
China health insurance landscape

China's healthcare industry and insurance sector - which is categorized under the finance industry, have been growing rapidly in recent years and outperforming other industries per GDP. It is expected that the total health expenditure in China will reach around RMB 6,214.7 billion (USD 955.8 billion) by 2020, representing an additional growth of RMB 2,100 billion, from RMB 4,097.5 billion in 2015.

We believe that there are five key market growth drivers in the country, namely, policy and regulation, aging population, middle class growth, urbanization and chronic diseases. Among which, the aging population of 65 and above is estimated to increase from 10.5 percent of the total population of over 1.3 billion in 2015, to approximately 25 percent by 2025. The Chinese middle class will also grow to 55 percent of the total population by 2020, from 16 percent in 2010, which will boost demand for insurance and healthcare services.

In addition, the rising incidence of chronic diseases, such as diabetes, with about 114 million diabetic patients (1 out of 3) in the world, comparing to only a 32 percent diagnosis rate in China and 73 percent in the US, will offer market growth opportunities to domestic insurers, MNCs and new local entrants to the Chinese health insurance sector.

Figure 1: Current healthcare ecosystem in Mainland China



When comparing with other countries in the global healthcare marketplace, China's total healthcare spend remains relatively low, while patients face steep out-of-pocket costs at the same time due to limited insurance coverage. Over time, the high out-of-pocket patient costs will lead to increasing demand for health insurance, which may then help relieve sub-optimal healthcare consumption, such as skipped care, over-the-counter reliance, poor adherence and limited preventative care that are currently existing in the local market.

We have seen significant growth but erratic profitability in China's healthcare ecosystem. Insurers, for example, currently have a growth rate of approximately 20 percent and are anticipated to have a strong expenditure growth over the next decade. However, their profitability is generally low due to lack of product differentiation, service and quality, while improvements in the sector are expected to be slow. Despite this, the market prospect of insurers, along with private hospitals and biotech companies, are continuously trending upwards in the overall healthcare ecosystem.

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Another challenge of China's health insurance market is the intense price competition, mainly due to undifferentiated products such as critical illness, lump sum products and expensive distribution channels – mostly through intermediaries. Insurers thus need to invest significantly in their agent and broker networks.

Three main categories of participants are also facing different types of key challenges. Domestic insurers find difficulties in product differentiation and profit growth, MNCs are tested by market penetration and provider network, while new local entrants are facing the challenges of market expansion, product differentiation and provider network.

Although the previous health reform in China quickly increased the number of health insurers – comprising local players and MNCs – by more than double between 2005 and 2015, with the total players expanding from 50 to 129; the market performance between local players and multinational players is varied.

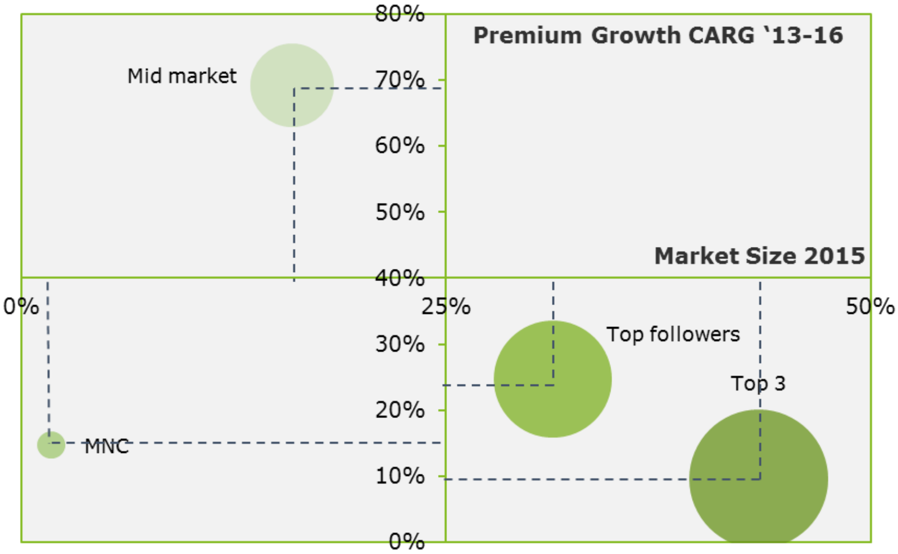
Historically, China's health insurance market has been dominated by a handful of top domestic companies, currently controlling over 30 percent combined market share. However, smaller and medium sized companies are now gradually catching up.

Turning our attention to MNCs, we have found that individual market share is mostly below the market average by size and growth with a market penetration rate of less than one percent, while these players are continuing to lose share. In the micro view, growth of MNCs remains low, and most of them sit within a narrow bandwidth of a 10-15 percent average CAGR.

With the exception of a few very large insurance players dominating health insurance distribution and service administration, value chain integration, however, remains a significant challenge among insurers in China. Finding alternative business models along the insurance aftermarket, or white space such as care management, care provision, care product distribution and care product production, is a key strategic objective of insurers.

Meanwhile, healthcare ecosystem integrations have begun to emerge in recent years. Partnerships with healthcare service providers are another way that insurers can effectively increase their customer base, control risk and costs, as well as allow them to maximize profitability.

Figure 2: Overview of players in China's health insurance market



Key trends and facts

"Top 3"	• Have traditionally controlled the market with over 30% market share combined • Recently losing market share as other players establish themselves
"Top followers"	• Above average sized companies • Catching up quickly with top 3 and will likely surpass them in overall market share 3- 4 years
"MNCs"	• Individual market shares are mostly below 1% • Continuing to lose share
"Mid market players"	• Small to mid-sized local companies • Key beneficiaries of strong overall market growth in recent years

With Chinese regulators previously allowing a local insurer to invest in a hospital, insurance companies have an opportunity to easily obtain patient data; valuable information which can help them price and design successful products, while lowering their risks and claims ratios. For example, a Beijing-based insurer has invested billions of renminbi to build a network of hospitals, eldercare communities and specialty facilities. Another nationwide insurer has built a 2,000-bed hospital in cooperation with the government[2].

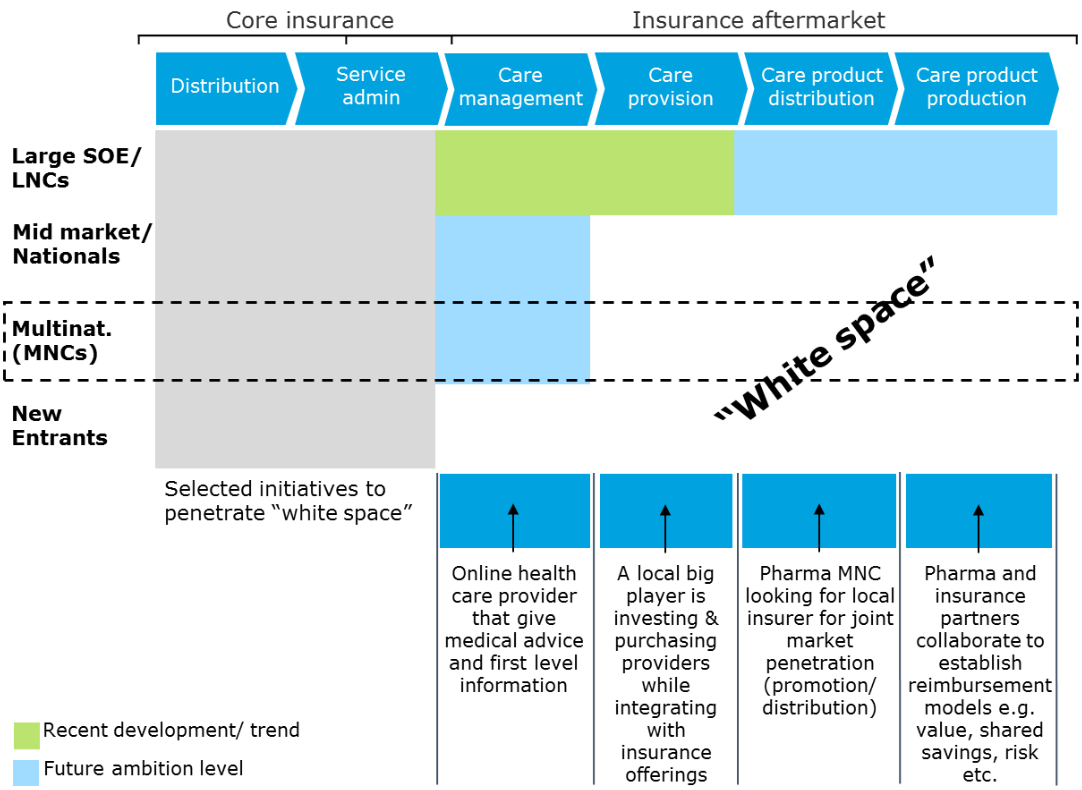
Future prospects

It is anticipated that in the next three years, health insurance market-dominant incumbents will continue to solidify their leading position by integrating horizontally, while sub-scale players like MNCs and new local entrants will need to find a way to enter the white space of the Chinese healthcare ecosystem. In order to capture these potential market segments, insurers need to take in-depth consideration when choosing the most effective access strategies, while identifying the right local partner for business collaboration.

Another feature of the Chinese healthcare market is that insurers have to account for the cost of the entire distribution network of pharmaceutical and device suppliers. It is therefore key for insurance companies to understand and manage these costs, which also provide potential business opportunities to MNCs and new local entrants.

With the attraction of high growth rates, the number of health insurers in the country will likely continuously increase. Besides incumbents, innovative aggressive players are expected to enter the market; six new local entrants have formed in China in the seven-year period between 2010 and 2017, including two online insurers and two health insurers under the same leading Chinese pharmaceutical conglomerate.

Figure 3: Trends among insurers managing Chinese healthcare ecosystem



In addition to focusing on market development, insurers in China can also leverage positive regulations and policies to promote business development in the private health insurance sector. At present, there are four favorable policies initiated by the State Council and the insurance regulator, the China Insurance Regulatory Commission (CIRC)[3], supporting local market growth in the sector. Those policies are:

- Encourage urban individuals to purchase private health insurance as supplement of government insurance;
- Encourage private insurance to co-manage government critical illness insurance program;
- Promote private health insurance by providing tax benefits to individuals; and
- Allow insurance fund to invest in venture capital.

As part of building a healthy China, the 13th Five-year Plan (2016-2020) proposal intends to change the health insurance system in order to protect people against high medical expenses. Between 2009 and 2014, the Chinese government spent RMB 4 trillion on health, among which RMB 1.2 trillion came from the central government. The medical insurance scheme now covers over 1.3 billion people, more than 95 percent of the total population. The government requires that health insurance will cover at least 70 percent of patients' medical expenditure by 2017.

Full-scale reform of the medical care system in China began in 2009. Pilot projects for public hospitals were a priority, along with a basic medical security system, improvements at the local level and equal access to basic public health services. In 2016, there were 993,000 medical and health institutions in China, including 29,000 hospitals. Of all the hospitals, 13,000 were public, and 16,000 were private, according to the National Bureau of Statistics of China[4].

Conclusion

The private health insurance industry is one of the most challenging, regulated and developing ecosystems in mainland China, where local big players are dominating the market. However, multinational insurers and new entrants can still overcome the entry barriers by formulating the right strategies and collaborating with the right local partner. MNCs and local new entrants should consider the white spaces in the market – care management, care provision, care product distribution and care product production – to penetrate this ecosystem. Insurers are also recommended to leverage their business partnerships for better consumer data collection, as well as effectively use analytics and technologies to derive insights from the data, so as to improve their future product design and pricing management.

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Contacts

Tim Pagett
Financial Services Leader, China
+852 2238 7819
tpagett@deloitte.com.hk

Gary Teh
Insurance Sector Leader, Hong Kong
+852 2531 1588
garyteh@deloitte.com.hk

Martin Wong
Insurance Sector Leader, Mainland China
+86 755 3353 8282
martiwong@deloitte.com.cn

David Wu
Partner, Consulting
+852 2238 7248
davidwwu@deloitte.com.hk

Joanna Wong
Partner, Consulting
+852 2852 6724
joawong@deloitte.com.hk

Kelly Zhou
Director, Deloitte Digital
+86 21 2316 6711
kzhou@deloitte.com.cn

Dr. Paul Sin
Partner, Consulting
+852 2852 6448
psin@deloitte.com.hk

Eric Lu
Partner, Consulting
+852 2238 7019
erilu@deloitte.com.hk

Simon Dai
Partner, Consulting
+852 2238 7348
simondai@deloitte.com.hk

Rebecca Ng
Manager, Consulting
+852 2852 5882
rebng@deloitte.com.hk