Healthcare BUSINESS STRATEGY™

Medicaid Market Growth Opportunities

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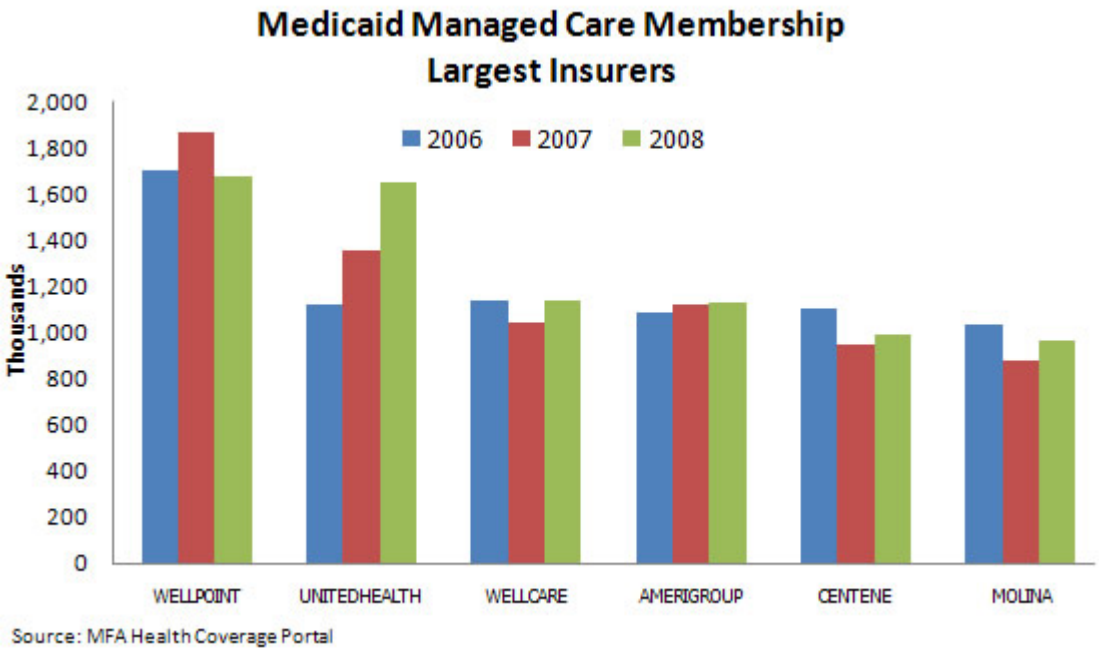
by Margaret E. Dick

The Medicaid market could be the silver lining in the economic storm cloud that has settled over health plan enrollment in the United States. Faced with increased unemployment and a continued decline in the employer-sponsored healthcare market, major players such as UnitedHealth Group are looking to the Medicaid market to help offset projected losses in commercial membership in 2009.

Since the current recession began in December 2007, the U.S. economy has shed 5.7 million jobs. That drop translates into lost commercial membership for health plans as job-based healthcare coverage disappears. UnitedHealth officials say the company could lose 1.5 million commercial members if the unemployment rate, which was 8.6% in April, reaches 10% in 2009. Meanwhile, demand is exploding for Medicaid coverage, including managed care. This report looks at the current state of the managed Medicaid market, including membership and key financial data for top Medicaid insurers, and discusses how new government policies are shaping opportunities for health plans in this arena.

Managed Medicaid Enrollment

About 125 insurers offer managed Medicaid health plans for 21 million recipients with the six largest insurers accounting for more than 36% of that membership. Among top insurers only WellPoint posted a membership loss from year-end 2007 to year-end 2008 and that reflects WellPoint's planned departures in 2008 from Medicaid markets in Connecticut and Ohio.



While there has been organic growth, health plans have been on buying sprees to boost their Medicaid and Children's Health Insurance Program (CHIP) members. Recent purchases include:

- Centene's acquisition of Community Care of South Carolina in March 2009, added 14,000 CHIP members to its Absolute Total Care subsidiary.
- UnitedHealth Group increased enrollment by 270,000 Medicaid members in 2008 when it acquired Unison Health Plans.
- Aetna obtained 600,000 Medicaid members in 2007 when it bought Schaller Anderson.
- Humana's acquisition of PHP Companies (doing business as Cariten Healthcare) from Covenant Health in 2008, included 93,000 Medicaid members. However, Cariten's Medicaid business, related to a TennCare contract, expired on December 31, 2008 and was not renewed.

Growing Federal Support

Insurers are optimistic about the potential for profitable growth in the Medicaid market thanks in part to the American Recovery and Reinvestment Act of 2009 (ARRA) and The Children's Health Insurance Program Reauthorization Act of 2009 (CHIPRA).

Tucked inside the American Recovery and Reinvestment Act commonly known as the federal economic stimulus package is an estimated $88 billion in assistance for state Medicaid programs. The bill provides a temporary increase in the Federal Medical Assistance Percentage (FMAP) from October 1, 2008 through December 31, 2010. That means states will receive additional federal matching funds for every dollar of state money earmarked for Medicaid. In spite of their own budget problems, most states will be less likely to cut Medicaid services due to the attractiveness of the increased federal funding from ARRA. FMAP promises of 56% to 87% reimbursement levels depending on the state are hard to ignore.

CHIPRA budgets $33 billion in federal funds to help provide medical coverage to an additional 4.1 million children by 2013. The Act also requires states to add dental services to CHIP and to offer mental health and substance abuse coverage in parity with medical and surgical benefits.

Moreover, the Federal Reserve Board, the Congressional Budget Office and some states have recognized the positive economic impact of Medicaid spending. Taking into account its multiplier effect, Medicaid spending supports jobs, incomes, purchases and state tax revenues. For example, North Carolina officials credit Medicaid spending with more than 67,000 jobs and $2.8 billion in income, according to a 2009 study by the Kaiser Commission on Medicaid and the Uninsured.

Movement toward Managed Medicaid

More states are expanding their managed Medicaid coverage beyond the traditional markets such as non-elderly adults, to more medically needy populations in an effort to help control costs and impose more performance measures. Some insurers see profitable managed care opportunities in the long-term care as well as the aged, blind and disabled (ABD) markets.

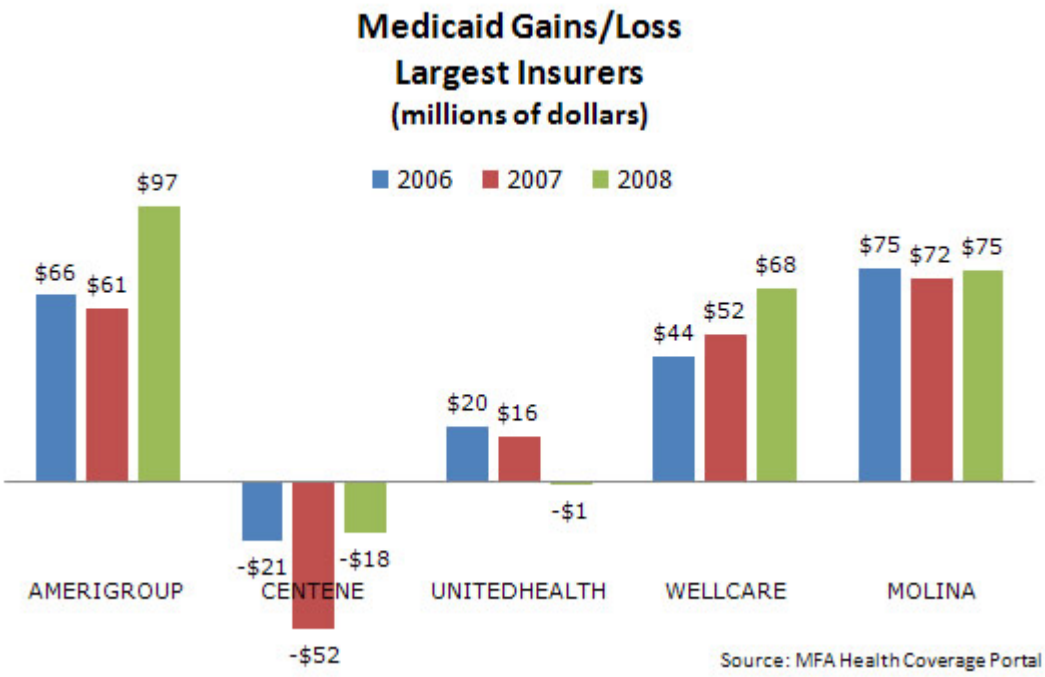
The ABD population represents about 24% of all Medicaid beneficiaries but accounts for about 70% of Medicaid spending. Only 20% of the aged, blind and disabled are in managed care programs. State officials see managed care as a way to provide more comprehensive and cost-effective care for a population that tends to develop complex medical problems. About 40 states are in the process of shifting at least a portion of their ABD fee-for-service clients into managed care programs. The trick for insurers is to move into the ABD market in states where payment rates keep pace with costs. WellPoint, WellCare and Centene, all major players in the Medicaid managed care marketplace, each pulled out of Ohio's ABD managed care program in 2008 citing financial losses when the state's rates failed to keep pace with their costs.

The Medicaid long-term care (LTC) market consists of the chronically ill and disabled. Like the ABD population, the LTC market presents the financial challenge of managing a population with a variety of illnesses and special needs. Much of this care has been provided in an institutional setting on a fee-for-service basis. Several states are shifting their LTC clients away from expensive institutional locations to home and community-based services. The care coordination model is being implemented in some states to plan and

arrange services to meet individual needs. In addition, some states are incorporating disease management into their LTC strategies presenting another opportunity for managed care plans. About 15 states have implemented LTC Medicaid managed care programs or are studying the opportunity.

Tight Grip on Expenses Necessary

There is plenty of money at stake with state and federal Medicaid spending totaling $319.7 billion in FY2007. CHIP spending was slightly more than $10 billion in FY2008. Nevertheless, seeing a positive return on investment by serving a medically vulnerable population requires a tight grip on medical expenses and administrative costs. An analysis of NAIC financial data from 2006 to 2008 shows mixed results for the largest Medicaid managed care insurers.



Three of the top plans, AMERIGROUP, WellCare and Molina, posted financial gains on their Medicaid business in 2008. Centene posted Medicaid-related loses for 2006, 2007 and 2008. WellPoint's Medicaid results are not comparable to the others because its financials do not include a breakout for the Medicaid segment for its Blue Cross of California health plan and have been excluded here. However, for the states where WellPoint does report Medicaid specific gains and losses, in total the company saw losses in 2007 and 2008 for this segment.

Medicaid-related revenues have been trending up from 2006 to 2008. Of the top insurers Amerigroup leads the group with revenue per member per month of $237.65. Centene, Molina and Wellcare all saw large increases between 2006 and 2007, bringing Centene on par with UnitedHealth.

Leading Plans' Medicaid Revenue PMPM					
Per Member Per Month (PMPM)	2006	2007	2008	Increase '06 to '07	Increase '07 to '08
AMERIGROUP	$205.80	$223.26	$237.65	8%	6%
UNITEDHEALTH	$203.56	$219.03	$233.76	8%	7%
CENTENE	$177.42	$219.43	$232.33	24%	6%
MOLINA	$132.91	$182.75	$201.17	37%	10%

WELLCARE	$163.92	$190.38	$198.48	16%	4%

Medical expense ratios (Medicaid medical expense divided by Medicaid revenues) are trending around the mid-80% level. Administrative expense ratios (Medicaid related administrative expense divided by Medicaid revenues) are trending between 12.8% for Molina and 16.3% for Centene.

Top Medicaid Plans Financial Ratios Medicaid Business as of December 31, 2008			
Parent	Med Exp/Rev	Adm Ex/Rev	Gain(Loss)/Rev
AMERIGROUP	81.2%	15.7%	3.1%
UNITEDHEALTH	87.0%	13.0%	0.0%
CENTENE	84.3%	16.3%	-0.7%
MOLINA	83.9%	12.8%	3.3%
WELLCARE	82.3%	15.1%	2.6%

These findings demonstrate that even the most experienced insurers find the Medicaid market challenging. While the increase in Medicaid eligibles creates opportunities, meeting the medical needs of this population, especially in the ABD and LTC markets, will require health plans to closely monitor related expenses, negotiate favorable contracts and keep an eye on government policy.

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