



GCR affirms Resolution Health Medical Scheme's rating of BBB-(ZA); Outlook Stable.

Johannesburg, 5 July 2016 — Global Credit Ratings has today affirmed the national scale claims paying ability rating assigned to Resolution Health Medical Scheme of BBB_(ZA), with the rating outlook accorded as Stable.

SUMMARY RATING RATIONALE

Global Credit Ratings ("GCR") has accorded the above credit rating to Resolution Health Medical Scheme ("Resolution") based on the following key criteria:

Resolution's earnings capacity is viewed to be moderate, although exposed to pressures going forward. The scheme has posted thin net healthcare surpluses of approximately R4m over the past two years, with a net result of R11m projected for FY16. Going forward, the rating exhibits sensitivity to potential earnings compression arising out of an elevated claims ratio (noting potential for high benefit utilisation, particularly given the rising average age profile), while the reducing scale of the contribution base may give rise to a degree of relative margin volatility.

Resolution's solvency is viewed to be low, and tracking well below original expectations, albeit evidencing an incrementally improving trend. The statutory solvency margin edged up to 10.4% in FY15 (FY14: 9.4%), although fell short of the target margin for the year of 12.9%. The solvency margin is forecast at 12.8% in FY16, as per the business plan, with full statutory compliance expected by management to be achieved by FY18. The targeted solvency trajectory has been factored into GCR's existing view of the scheme's credit profile. Accordingly, the capacity of the scheme to successfully execute the business plan, and achieve short term financial targets, represents a key rating consideration over the rating horizon.

Resolution's membership base evidences a higher rate of member outflow relative to expectations, coupled with a rising average age. The membership base stood at 19,587 at 1Q F15, with consecutive membership losses since FY12 totalling 21,137. The shrinking membership base is viewed with concern. This is due to the deterioration in the scheme's risk profile due to the rise in the average age (deteriorating by three years to 47 in FY15), the reduction in membership diversification, and the reducing scale of the contribution base relative to claims in absolute terms.

Liquidity is viewed to be intermediate. Key liquidity metrics, while still constrained, have stabilised, and are expected to remain within a similar range over the short term. The relatively low scale of the cash balance (FY15: R115m) reflects a comparatively lower capacity to absorb claim spikes. The scheme adopts a conservative asset allocation strategy, which mitigates balance sheet exposure to asset risk.

Upward rating action could develop over the medium term from the consistent generation of net surpluses, underpinning materially enhanced reserves and associated key credit protection metrics. Stabilisation of membership volumes may also lend increased steadiness to the scheme's



performance, potentially contributing towards positive rating movement. Negative rating action may follow a deviation in Resolution's performance relative to expectations. Negative membership base trends (with respect to outflows and age profile) may also have a negative rating impact. The rating will be adversely affected by a weakening of liquidity and solvency metrics.

NATIONAL SCALE RATINGS HISTORY
Initial rating (June 2004)
Claims paying ability: A ⁻ _(ZA)
Outlook: Positive
Last rating (April 2015)
Claims paying ability: BBB ⁻ _(ZA)
Outlook: Stable

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APPLICABLE METHODOLOGIES AND RELATED RESEARCH

Criteria for Rating Medical Schemes, updated April 2015

Resolution Health Medical Scheme rating reports, 2004-2015

RATING LIMITATIONS AND DISCLAIMERS



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SALIENT FEATURES OF ACCORDED RATINGS

GCR affirms that a.) no part of the rating was influenced by any other business activities of the credit rating agency; b.) the rating was based solely on the merits of the rated entity, security or financial instrument being rated; c.) such rating was an independent evaluation of the risks and merits of the rated entity, security or financial instrument; and d.) the validity of the rating is for a maximum of 12 months, or earlier as indicated by the applicable credit rating document.

Resolution Health Medical Scheme participated in the rating process via face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The credit rating has been disclosed to Resolution Health Medical Scheme with no contestation of the rating.

The information received from Resolution Health Medical Scheme and other reliable third parties to accord the credit rating included:

- Unaudited financial results to 31 December 2015
- Four years of comparative numbers
- Unaudited interim results to 31 March 2016
- Budgeted financial statements for 2016
- Other related documents

The rating above was solicited by, or on behalf of, the rated client, and therefore, GCR has been compensated for the provision of the rating.

GLOSSARY OF TERMS/ACRONYMS USED IN THIS DOCUMENT AS PER GCR'S INSURANCE GLOSSARY

Accounting	A process of recording, summarising, and allocating all items of income and expense of the company and analysing, verifying and reporting the results.
Cash	Funds that can be readily spent or used to meet current obligations.
Claim	A request for payment of a loss, which may come under the terms of an insurance contract.

Credit rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Intermediary	A third party in the sale and administration of insurance products.
Investment portfolio	A collection of investments held by an individual investor or financial institution.
Liquidity	The speed at which assets can be converted to cash. The ability of an insurer to convert its assets into cash to pay claims if necessary. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Loss	The happening of the event for which insurance pays.
Operating result	The sum of underwriting result and investment income.
Portfolio	All of the insurer's in-force policies and outstanding losses, with respect to described segments of its business.
Rating horizon	The rating outlook period
Reserve	(1) An amount representing actual or potential liabilities kept by an insurer to cover debts to policyholders. (2) An amount allocated for a special purpose. Note that a reserve is usually a liability and not an extra fund. On occasion a reserve may be an asset, such as a reserve for taxes not yet due.
Retention	The net amount of risk the ceding company keeps for its own account.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Solvency	With regard to insurers, having sufficient assets (capital, surplus, reserves) and being able to satisfy financial requirements (investments, annual reports, examinations) to be eligible to transact insurance business and meet liabilities.
Statutory	Required by or having to do with law or statute.
Statutory solvency margin	Gives an indication as to whether the minimum regulatory solvency margin is being met, based on the net statutory assets to statutory net premiums ratio.

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