



## GCR assigns an initial national scale financial strength rating of A+<sub>(ZA)</sub> to Government Employees Medical Scheme; Outlook Positive

### Rating Action

Johannesburg, 20 November 2019 - GCR Ratings ("GCR") has assigned a national scale financial strength rating to Government Employees Medical Scheme ("GEMS") of A+<sub>(ZA)</sub>, with the outlook accorded as Positive.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook/Watch
Government Employees Medical Scheme	Financial strength	National	A+ <sub>(ZA)</sub>	Positive Outlook

### Rating Rationale

GEMS's national scale financial strength rating reflects the scheme's large and captive membership base and moderately strong liquidity, which is partially offset by the very limited track record of earnings and solvency management, as well as high sectoral concentration.

Liquidity is viewed to be moderately strong, with stressed financial assets coverage of average monthly claims and operational cash coverage registering at 3.95 months and 1.07x at FY18 respectively. Earnings have improved discernibly over the past two years, albeit constrained by review period volatility in performance. Cumulative net healthcare surpluses for FY17 and FY18 amounted to R6.3bn, compared to the prior three-year cumulative net healthcare deficits of R1.4bn. Looking ahead, while operating results may moderate (relative to FY17 and FY18) on the back of contained average contribution increases, ongoing cost containment may continue to support a healthy earnings trajectory. Nonetheless, the earnings assessment is moderated by a limited track record of sustained financial performance, and the scheme's ability to maintain consistently positive net healthcare results will be a key rating consideration going forward.

The rebound in the scheme's earnings over the past two years has facilitated an accelerated pace of reserve accumulation. GEMS's statutory solvency margin registered at a review period high of 24.7% at FY18, while the year to date result reflects continued strong financial performance in FY19, thereby supporting the view of attaining statutory compliance by the end of FY19. Cognisance is, however, taken of the limited solvency management track record, and the associated execution risk in sustaining the positive trend over a prolonged period, which moderates the solvency assessment.

GEMS's membership profile is viewed to be strong, underpinned by a large membership base and a favourable age profile. Moreover, GEMS benefits from a fairly stable captive membership pool.

Going forward, the membership profile is expected to remain positive to the rating.

Notwithstanding the above, GCR views the high concentration to the public sector as a rating weakness, given the scheme's exposure to inherent systematic risks, which moderate the membership profile assessment.

### Outlook Statement

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The Positive Outlook reflects the strengthening in the scheme's financial profile, which, if sustained, could support upward rating movement.

### Rating Triggers

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While downward rating movement is considered unlikely over the short term, a material and sustained deterioration in earnings, negatively impacting solvency, could lead to negative rating action.

### Analytical Contacts

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### Related Criteria and Research

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Criteria for the GCR Ratings Framework, May 2019
Criteria for Rating Insurance Companies, May 2019
GCR Ratings Scales, Symbols & Definitions, May 2019
GCR Country Risk Scores, June 2019
GCR South African Medical Schemes Sector Risk Score, September 2019

### Ratings History

Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Financial Strength	Initial	National	A+ <sub>(ZA)</sub>	Positive	November 2019
	Last	National	A+ <sub>(ZA)</sub>	Positive	November 2019

### Risk Score Summary

Risk scores	Government Employees Medical Scheme
<b>Operating environment</b>	<b>15.50</b>
Country risk score	7.50
Sector risk score	8.00
<b>Business profile</b>	<b>0.50</b>
Membership profile	0.50
Management and governance	0.00
<b>Financial profile</b>	<b>-0.25</b>
Earnings	-0.25
Capitalisation	-0.50
Liquidity	0.50
<b>Comparative profile</b>	<b>0.00</b>
Peer analysis	0.00
<b>Total Score</b>	<b>15.75</b>

### Glossary

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.
Rating Horizon	The rating outlook period
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
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.
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 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.
Statutory	Required by or having to do with law or statute.

#### SALIENT POINTS OF ACCORDED RATING

GCR affirms that a.) no part of the rating process 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; and c.) such rating was an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit rating has been disclosed to Government Employees Medical Scheme. The rating above was solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the rating.

Government Employees Medical Scheme participated in the rating process via face-to-face management meetings, and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from Government Employees Medical Scheme and other reliable third parties to accord the credit rating included:



The audited financial results up to 31 December 2018  
Four years of comparative audited numbers to 31 December  
Unaudited interim results up to 31 August 2019  
Budgeted financial statements to 31 December 2019  
Other related documents.