

2020 half year results

Customer focus delivers stronger policyholder growth

CEO COMMENTARY

“Despite some challenges in the first half of 2020, focusing on delivering a better customer experience has continued to deliver growth in our business.

“Strong Service NPS for both Medibank and ahm has enabled us to maintain momentum in policyholder growth with a net increase of 11,700 resident policyholders in the first half, delivering an 8 basis point increase in our market share.

“Today’s result also reflects the continuation of the higher claims environment we saw in the second half of 2019 and the investment in customer benefits such as our new Members’ Choice Advantage dental network.

“The key driver of claims growth was a 6.4% increase in prostheses cost, which was responsible for 69% of the increase of growth in hospital claims. This is extraordinary given a subdued 1.1% increase in hospital utilisation for the half.

“We are continuing to manage affordability and claims through a range of initiatives such as payment integrity, contract management and in-home care and advocating for wider reform of the industry.

“The issues that exist in the private health system are well known and we continue to lead the way in driving more reform.

“While the Government has taken progressive steps in implementing reforms, which have had some positive impact on the system, there must be recognition that additional meaningful industry cost savings and enhanced industry participation can only be realised through new Government reforms.

“That said, Medibank and the broader health system, including payors and providers, have an ongoing obligation and challenge to remove unnecessary costs from the system to ensure the future sustainability of our world class health system.

“In order to deliver affordable and sustainable care that meets customers’ changing demands, we are focused on supporting alternative settings for delivering care, giving customers greater choice and enhancing patient experience.

Investor briefing

The investor briefing will be held today at 9.30am AEDT. The investor presentation and webcast will be accessible on Medibank’s [investor centre](#). Video interviews with CEO Craig Drummond and CFO Mark Rogers are available on our [newsroom](#).



Key numbers

\$2.9b

benefits paid to customers

\$178.6m

Group net profit after tax

+11,700

net resident policyholders since 30 June 2019

5.70

cents per share

interim dividend fully franked

Strong growth in customer advocacy

30.7

Medibank average Service NPS
(+7.1 compared to 1H19)

40.7

ahm average Service NPS
(+5.2 compared to 1H19)

Financial summary

Group NPAT \$178.6 million, down 9.0% from \$196.3 million

Group operating profit \$218.8 million, down 20.9%

Health Insurance

- Operating profit of \$224.2 million, down 20.4%
- Premium revenue growth of 2.3%
- Management expense ratio of 7.5%, down from 8.5% in 1H19

Medibank Health

Operating profit of \$13.3 million, up 5.6%

Net investment income \$38.5 million, up from \$4.1 million in 1H19 in line with benchmark indices

*Numbers presented on a continuing basis unless otherwise indicated

“The expansion of our in-home care capability has seen 4,100 patients utilise hospital in the home or rehab in the home in the first half, of which more than 2,500 were Medibank customers.

“We have done this while taking costs out of our own business and introducing more value for our customers in our products.

“Our Health Insurance costs are down 9.6% for the half, meaning that we have delivered an additional \$10 million in productivity savings over the last six months, and are on track for our full year target of \$20 million.

“We are working hard within our business to address the challenges, but Government and the broader private health industry must play a meaningful role to ensure that additional reforms happen as soon as possible. An absence of reform this year could further deepen the prudential regulator’s concerns regarding the overall sustainability of the industry.”

CRAIG DRUMMOND
CHIEF EXECUTIVE OFFICER

Dividend

The Board has determined an interim dividend of 5.70 cents per share, fully franked. The interim dividend represents an 88% payout ratio of underlying NPAT from total operations. Given our strong capital position, we expect the payout ratio for the full year to be at the top end or above our target 75% to 85% payout range of underlying NPAT, normalising for investment returns.

2020 interim dividend dates

Ex-dividend Date	 3	Tuesday March 2020
Record Date	 4	Wednesday March 2020
Payment Date	 26	Thursday March 2020

PERFORMANCE IN DETAIL

Group

Group NPAT decreased by 9.0% to \$178.6 million (1H19: \$196.3 million). This was due to the reduction in Health Insurance operating profit, but partially offset by an increase in net investment income.

Health Insurance

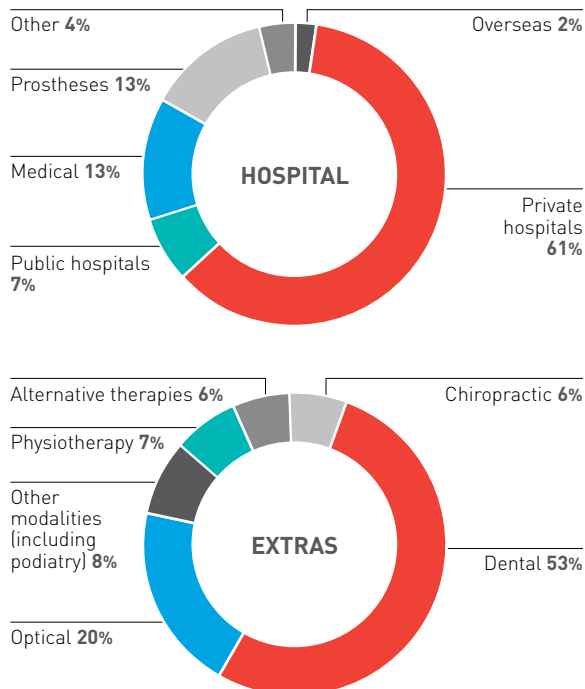
Health Insurance operating profit decreased 20.4% to \$224.2 million (1H19: \$281.5 million). This was driven by the continued higher claims environment and investment in customer benefits such as the new Members’ Choice Advantage dental network.

Premium revenue was up 2.3% to \$3.3 billion. At a fund level, there was a net increase in resident policyholders of 11,700 or 0.7% in the first half, with improvements in the rate of acquisition and retention. Medibank retention continued to improve supported by the Live Better rewards program and Members’ Choice Advantage dental and optical networks. The ahm brand continued to grow, with policyholder growth of 4.2%.

Net claims increased by 5.9% to \$2.8 billion due to a \$151.9 million increase in claims expense and a \$6.8 million reduction in risk equalisation receipts. Hospital claims were 6.0% higher with growth in prostheses the major driver. Extras claims were 5.6% higher, driven by investment in the Members’ Choice Advantage dental network, although this growth was partially offset by lower growth in natural therapies following regulatory reform.

Management expenses decreased by 9.6% to \$248.1 million, with the management expense ratio (MER) improving from 8.5% to 7.5%. We are targeting \$50 million of productivity savings across the next three years and we are on track to deliver \$20 million in savings in FY20.

COMPOSITION OF CUSTOMER CLAIMS



Medibank Health

Operating profit was up 5.6% to \$13.3 million. Medibank Health revenue was up 18.1% to \$128.6 million (1H19: \$108.9 million), which includes a full six months of contribution from Home Support Services (acquired in August 2018) and the new Live Better rewards program (launched in August 2019). Management expenses increased by 12.5% which includes additional investment in the home care business and Live Better, partially offset by \$4.0 million in cost savings.

Investment income

Net investment income increased from \$4.1 million to \$38.5 million in 1H20 with higher returns from both the growth and defensive portfolios. Consistent with previous practice, in order to calculate underlying NPAT for the purpose of determining the dividend for the period, we have adjusted net investment income to normalise for the impact of short-term market movements. After normalisation, the 1H20 net investment income was \$39.7 million, marginally down from \$39.9 million in 1H19.

Capital

Health Insurance related capital as at 31 December 2019 was \$872.8 million, representing 13.0% of premium revenue, which is at the top end of the Board's stated target range of 11.0% to 13.0%.

OUTLOOK

- On the current trajectory, we continue to expect Medibank brand volumes to stabilise by the end of FY20 and grow during FY21
- We expect hospital and ancillary utilisation to remain around current levels for the remainder of FY20
- We also expect approximately 3% underlying claims growth per policy unit for FY20
- Management expenses are expected to be approximately \$540 million for FY20
- We have made good progress on our productivity program and will provide an update at the FY20 result as we continue to investigate other opportunities
- We are confident that Health Insurance earnings will be higher in the second half of FY20
- Targeted inorganic growth for Medibank Health and Health Insurance remain areas of focus
- We expect our dividend payout ratio to be at the top end or above our revised target range of 75% to 85% of underlying NPAT from total operations for FY20
- We will review our capital management options with our FY20 results
- Our intention remains to aspire for stronger growth in volumes at a reasonable margin

FURTHER ENQUIRIES

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All figures are in Australian dollars unless stated otherwise. Some figures, amounts, percentages, estimates, calculations of value and fractions are subject to rounding. Accordingly, the actual calculations of these figures may differ from figures set out in this document. Further, some balances subject to rounding, may not add consistently throughout the document.

SUMMARY OF FINANCIAL RESULTS

Six months ended 31 December (\$ million)	1H20	1H19	Change
Group:			
Revenue from external customers ¹	3,421.5	3,330.8	2.7%
Health Insurance operating profit	224.2	281.5	(20.4%)
Medibank Health operating profit ¹	13.3	12.6	5.6%
Segment operating profit	237.5	294.1	(19.2%)
Corporate overheads	(18.7)	(17.4)	7.5%
Group operating profit – continuing operations	218.8	276.7	(20.9%)
Net investment income	38.5	4.1	n.m.
Amortisation of intangibles	(4.5)	(3.8)	18.4%
Other income/(expenses)	1.8	(2.9)	n.m.
Profit before tax	254.6	274.1	(7.1%)
Income tax expense	(76.0)	(77.8)	(2.3%)
NPAT – continuing operations	178.6	196.3	(9.0%)
NPAT – discontinued operations	(0.7)	11.4	n.m.
NPAT – total operations	177.9	207.7	(14.3%)
EPS (cents) ²	6.5	7.5	(14.3%)
Underlying NPAT – total operations³	178.7	232.8	(23.2%)
Underlying EPS – total operations (cents) ³	6.5	8.5	(23.2%)
Dividend per share (cents)	5.70	5.70	-
Dividend payout ratio ⁴	88%	67%	31.3%
Health Insurance:			
Premium revenue	3,315.5	3,240.3	2.3%
Net claims expenses (including risk equalisation)	(2,843.2)	(2,684.5)	5.9%
Gross profit	472.3	555.8	(15.0%)
Gross margin (%)⁵	14.2%	17.2%	(300bps)
Management expenses	(248.1)	(274.3)	(9.6%)
Management expense ratio (%)⁵	7.5%	8.5%	(100bps)
Operating profit	224.2	281.5	(20.4%)
Operating margin (%)⁵	6.8%	8.7%	(190bps)

1 Excludes discontinued operations. Discontinued operations relate to the Garrison Health Services contract which ceased on 30 June 2019.

2 Calculated on total operations.

3 Adjusted to normalise growth asset returns, including property from FY20, to historical long-term expectations and credit spread movements.

4 Dividend payout ratio based on underlying NPAT – total operations.

5 Includes Australian residents, OSHC and OVHC. The gross margin for Australian residents only was 16.5% in 1H19 and 13.8% in 1H20, the MER for Australian residents only was 8.1% in 1H19 and 7.3% in 1H20, and the operating margin for Australian residents only was 8.4% in 1H19 and 6.5% in 1H20.