Private Healthcare Market in Russia: Outlook for 2017-2019

KPMG Survey Results
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Welcome to our latest survey of the Russian commercial healthcare market. Here you will find our evidence-backed assessment of how the macroeconomic situation and public healthcare policy is affecting the private medical care market in Russia. The main goal of this survey is to analyse the current situation and identify the key trends that will drive the market over the next 2–3 years.

Based on our analysis of data and interviews with experts, we have identified several areas in which private healthcare providers can maintain and expand their market positions, by paying attention to the key factors driving market changes and trends in the competitive environment, as well as taking advantage of opportunities for public-private partnerships.

Please enjoy discovering the results of our analysis. We hope that this report will prove useful for you.

Best regards,

Victoria Samsonova
The Russian economy is forecast to come out of recession in 2017, though GDP growth rates are expected to remain low over the next few years. The proportion of government spending on healthcare to GDP is expected to increase insignificantly, up to 3.5–3.6% in 2017–2019.

Given the wider context of weak economic growth, the Ministry for Economic Development of the Russian Federation forecasts a decrease in inflation to 4% as early as 2017. At the same time, prices for healthcare services will grow faster than the consumer price index: in 2017, prices are expected to grow by 5.6%.

The Federal Obligatory Medical Insurance Fund will continue to occupy around 57–59% of the consolidated budget’s expenditure on healthcare, though the problems with collecting social insurance contributions will persist. However, any new legislation in this area, such as restricting the access of those who do not pay contributions for obligatory medical insurance, is very unlikely before 2019.

We expect players in the obligatory health insurance segment to continue the consolidation trend, as it is getting harder for small regional providers to compete with market leaders. Adding to this problem is a legislative change, raising the minimum charter capital needed by health insurers from 60 to 120 million roubles (from USD1.1 mln to USD2.1 mln)*.

The market for voluntary medical insurance in its current setup has reached saturation point. The share of voluntary medical insurance in the paid healthcare segment will drop from 20.1% in 2016 to 19.2% in 2019. Demand from corporate clients is not expected to increase, though the private client segment may become a source of growth in the medium term.

Given the reduction in real disposable cash income, more and more private healthcare providers are treating the obligatory medical insurance segment as a source of additional revenue. In 2016, private firms comprised 29% of the total number of healthcare providers operating in the obligatory medical insurance segment.

However, the high cost of debt is holding back PPP investment projects. The decline in the rate of inflation in 2017 and the resulting reduction in the cost of borrowing, will boost PPP investment projects in the healthcare market.

* According to the official foreign exchange rate of the Central Bank of Russia at June 10, 2017.
After two years of recession, the Russian economy is again expected to grow, but only slightly. The Ministry for Economic Development forecasts that Russian GDP will increase by 0.6% in 2017. While this is a sign of stabilisation, it does not give grounds for hoping for a significant improvement in the macroeconomic situation in the coming years.

Despite the significant economic turbulence and reduced federal spending on health, the total share of spending on health from the Russian Federation’s consolidated budget and the state’s extra-budgetary funds in 2012–2016, remained relatively stable, ranging from 3.3–3.5% of GDP. Projected growth in spending in 2018–2019 is most likely connected to the next electoral cycle, and may cease after the elections.

GDP changes and the share of consolidated budget expenditure on health in GDP, 2012–2019, %

Sources: the Federal State Statistics Service, the Ministry for Economic Development of the Russian Federation, the Federal Obligatory Medical Insurance Fund, KPMG analysis


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One of the most significant negative macroeconomic factors affecting the private healthcare market was the continuous fall in real disposable income in 2014–2016.

The impact of this was compounded by the fact that prices for medical services grew faster than the consumer price index. Throughout this period, with the exception of 2015, the difference in their growth rates ranged from about 0.6–7.2 percentage points.

Inflation will remain the key growth driver in the medical services market. According to BusinesStat forecasts, this will continue, with the rise in prices for medical services slightly outstripping changes in the consumer price index in 2017–2019. This will reign in the increase in demand for commercial health care, despite the slow recovery of the Russian economy and gradual revival of growth in household incomes starting from 2017, as the income growth rate will be too low to significantly stimulate demand for private medical services.

### Changes in the consumer price index and the medical services price index, 2012–2019, %

<table>
<thead>
<tr>
<th>Year</th>
<th>Consumer price index at the end of the year, %</th>
<th>Index of the average price for a medical appointment at the end of the year, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>104.0</td>
<td>104.5</td>
</tr>
<tr>
<td>2018</td>
<td>104.0</td>
<td>103.7</td>
</tr>
<tr>
<td>2017</td>
<td>104.0</td>
<td>104.6</td>
</tr>
<tr>
<td>2016</td>
<td>105.4</td>
<td>107.4</td>
</tr>
<tr>
<td>2015</td>
<td>109.5</td>
<td>112.9</td>
</tr>
<tr>
<td>2014</td>
<td>111.4</td>
<td>112.0</td>
</tr>
<tr>
<td>2013</td>
<td>106.5</td>
<td>113.7</td>
</tr>
<tr>
<td>2012</td>
<td>106.6</td>
<td></td>
</tr>
</tbody>
</table>

**Sources:** Ministry for Economic Development of the Russian Federation, BusinesStat, KPMG analysis

During the period under review, the share of consolidated budget expenditure in the total healthcare expenditure gradually decreased from 85% in 2012 to 81% in 2016, whereas the share of private segment spending grew. In the coming years, the cost structure will not undergo significant changes, and the increase in government spending planned for 2017–2019 will halt the decline in consolidated budget spending.

At the same time, the structure of consolidated budget expenditure on healthcare in Russia has changed significantly during the period under review. The shift towards single-channel financing has led to a significant increase in the expenses incurred by the Federal Obligatory Medical Insurance Fund (FOMIF), from 41% in 2012, to 59% in 2016; and a decrease in the share of federal budget expenditures, from 27% in 2012 to 16% in 2016. Financing coming from other sources, including the consolidated budgets of the regions of the Russian Federation, has also significantly increased.

The growth of FOMIF expenses risks a decrease in the quality and accessibility of medical care, due to underfunding. The acute nature of this issue is growing, and the government is now considering various measures aimed at balancing the FOMIF budget. For example, in October 2016, the Ministry of Health increased the rate of obligatory health insurance contributions from 5.1% to 5.9% from 2019 onwards, and abolished the so-called ‘reverse transfer’ from the FOMIF to the federal budget of 96.7 billion roubles (USD 1.7 billion). In December 2016, the Ministry of Finance proposed limiting the growth of healthcare professionals’ salaries in 2017 (to 5.4% instead of 10.6%), thus repairing the FOMIF budget deficit. However, the State Duma of the Russian Federation did not support this proposal. Later, in 2017, Vladimir Putin stressed the importance of completing the task that had previously been set of increasing the salaries of public sector physicians to up to 200% of the average level of earnings in the region in which they work.

### Structure of the Russian Federation’s consolidated budget expenditure on healthcare, 2012–2019

<table>
<thead>
<tr>
<th>Year</th>
<th>FOMIF expenses, billion RUB</th>
<th>Federal budget, billion RUB</th>
<th>Other, billion RUB</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>932</td>
<td>2,283</td>
<td>32</td>
</tr>
<tr>
<td>2013</td>
<td>1,049</td>
<td>2,318</td>
<td>27</td>
</tr>
<tr>
<td>2014</td>
<td>1,269</td>
<td>2,533</td>
<td>22</td>
</tr>
<tr>
<td>2015</td>
<td>1,638</td>
<td>2,861</td>
<td>18</td>
</tr>
<tr>
<td>2016</td>
<td>1,689</td>
<td>2,864</td>
<td>16</td>
</tr>
<tr>
<td>2017</td>
<td>1,735</td>
<td>3,034</td>
<td>12</td>
</tr>
<tr>
<td>2018</td>
<td>1,912</td>
<td>3,300</td>
<td>12</td>
</tr>
<tr>
<td>2019</td>
<td>2,022</td>
<td>3,551</td>
<td>10</td>
</tr>
</tbody>
</table>

**Sources:** the Federal Treasury, the Federal State Statistics Service, the Ministry for Economic Development of the Russian Federation, the Federal Obligatory Medical Insurance Fund, KPMG analysis

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Structure of healthcare expenditure, 2012–2019

Sources: Federal State Statistics Service, the Ministry for Economic Development of the Russian Federation, the Federal Obligatory Medical Insurance Fund, BusinesStat, KPMG analysis

http://www.finmarket.ru/main/article/4393971
4. http://www.rbc.ru/politics/05/12/2016/5845b2649a79479d98a3c9fb
http://www.kommersant.ru/doc/3236713

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Market trends

Obligatory medical insurance

The health insurance market continues to experience consolidation, as smaller players leave the market or are acquired by the leading health insurance providers.

For example, in 2016, ROSNO-MS became the property of VTB Insurance, and Astro-Volga-Med (Samara) was acquired by MAKS-M. This trend continued in 2017: in January, the health insurance companies Soglasie-M and Bashkortostan ceased operations, and at the beginning of February, RESO-Garantia filed an application with the Federal Antimonopoly Service of Russia to acquire 100% of the voting shares of MSK Uralsib.

Further concentration in the obligatory health insurance segment has been caused by the regulatory change resulting in additional expenses. These costs have primarily come via the introduction of insurance attorneys and a mandatory requirement for the charter capital of health insurance companies to be increased.

The insurance attorneys are supposed to ensure that health insurance providers create added value for patients. Introduced in 2016, they aim to act like personal managers for obligatory medical insurance patients, strengthening the functions and role of the insuring firm. However, they also increase the insurers’ expenses.

The increase in the charter capital of health insurers from 60 to 120 million roubles raises the threshold for those trying to enter the medical insurance market. The increase is provided for by the Federal Law No. 432-FZ of 30 December 2015, which introduced amendments to the laws governing insurance market in Russia and, in particular, the obligatory medical insurance.

Increase in the minimum charter capital of health insurers

60 million roubles

120 million roubles

http://www.wedomosti.ru/finance/news/2017/02/14/77621-reso-garantiya
http://www.banki.ru/news/daytheme/?id=5469169
In nominal terms, the voluntary health insurance segment continued to grow in 2016, though the one (6.7%) was lower than the one in the ‘legal’ commercial healthcare segment (9.1%), and than in the shadow (‘illegal’) segment (7.3%). This lower growth was a result of reduced demand for voluntary health insurance and the desire among policyholders to save money, choosing insurance programmes with less coverage.

In 2014–2016, the demand for insurance programmes from large enterprises – the main consumers of voluntary health insurance programmes – saw no fall in demand. However, at the same time, many of these companies optimised their headcount, and saved on voluntary health insurance costs by reducing the range of medical services provided to employees, for example, by eliminating costly or additional options, and by narrowing the list of available healthcare providers.

There was a considerable decrease in demand for voluntary medical insurance among medium-sized businesses, some of which ceased to provide voluntary health insurance programmes to their employees. However, the number of firms refusing to provide voluntary health insurance is low. The segment was supported by the Law No. 409-FZ, requiring migrant workers to have a voluntary health insurance policy; though the effect of this law on the total volume of the segment was not significant.

Summarising, it appears that the voluntary medical insurance segment in its present form has reached saturation point, as demand from large corporate customers is not expected to increase in the absence of economic growth.

Any growth that does occur will probably be driven by individuals seeking insurance, though that in turn depends on the availability of more attractively priced offers. The prime clients for this would be employees in medium-sized enterprises who have been deprived of their corporate voluntary medical insurance policies. Some of these patients have moved to the ‘legal’ commercial healthcare segment, though an increase in the availability of attractive voluntary health insurance programmes in the market could change their behaviour.
In the foreseeable future, the inflow of new patients – primarily into the lower-priced segment – into the legal commercial healthcare segment (as opposed to the shadow, illegal, segment) will continue. This is due to the declining availability of medical care in the obligatory health insurance segment (especially in the primary care sphere as a result of increased workloads), and the decrease in insurance coverage under corporate voluntary medical insurance policies.

The share of legal commercial healthcare in the paid medical services segment will continue to grow, reaching 57% in the coming years.

Self-employed individuals who currently evade taxation, yet enjoy social benefits, are also potential consumers of private healthcare services. According to different sources (the Russian Presidential Academy of National Economy and Public Administration, ‘Vedomosti’ newspaper), there were 13–16 million people who fit into this category in Russia in 2016. The Russian Ministry of Labour is considering limiting the access of these individuals to the obligatory medical system. The need to pay for obligatory healthcare will inevitably push some of these people into the legal commercial healthcare or voluntary health insurance segments. However, it is highly unlikely that these measures will be implemented before the end of 2018.

Foreign citizens represent another prominent group of clients for Russian healthcare players in the legal commercial segment. The fall in the value of the rouble has made medical treatment in Russia cheaper: favourable conditions for growth in the number of inbound medical tourists. That said, much effort is needed to promote the services of Russian healthcare providers abroad, both by individual clinics and hospitals and by their wider associations, in order to attract significant numbers of foreign patients to the Russian Federation.

The rapid development of information technology, and changes in related legislation, will also support growth in the legal commercial healthcare segment. This includes the launch of applications allowing users to search for healthcare providers or for doctors, such as Yandex.Health, or maintaining electronic medical records, such as via ONDOC, as well as adoption of the law on telemedicine.
By “shadow segment”, we mean unofficial payments made by patients to their medical carers, most often made directly in cash to the person caring, in order to receive more or better quality services.

The shadow segment size as part of the paid medical services segment gradually decreased in the pre-crisis period, reaching 24% in 2013. However, it then grew to 25% in 2014. This growth was caused by various factors, such as reduction in the availability of medical services in the obligatory health insurance system, decreases in the number of people having voluntary health insurance policies, and a fall in real disposable income. Costs in the shadow segment tend to be lower than in the voluntary health insurance and legal commercial medicine segments, so patients aiming to save money prefer to make direct payments to their medical staff.

Structure of the Russian market for paid medical services in 2012–2019

<table>
<thead>
<tr>
<th>Year</th>
<th>Shadow Segment</th>
<th>Voluntary Health Insurance</th>
<th>Legal Commercial Medicine</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>19%</td>
<td>23%</td>
<td>57%</td>
</tr>
<tr>
<td>2018</td>
<td>19%</td>
<td>24%</td>
<td>57%</td>
</tr>
<tr>
<td>2017</td>
<td>20%</td>
<td>24%</td>
<td>56%</td>
</tr>
<tr>
<td>2016</td>
<td>20%</td>
<td>25%</td>
<td>55%</td>
</tr>
<tr>
<td>2015</td>
<td>20%</td>
<td>25%</td>
<td>55%</td>
</tr>
<tr>
<td>2014</td>
<td>22%</td>
<td>25%</td>
<td>53%</td>
</tr>
<tr>
<td>2013</td>
<td>24%</td>
<td>24%</td>
<td>52%</td>
</tr>
<tr>
<td>2012</td>
<td>26%</td>
<td>24%</td>
<td>50%</td>
</tr>
</tbody>
</table>

Sources: BusinessStat
PPP in healthcare

As real disposable income fell in 2014–2016, private healthcare providers had to seek new sources of income. One of these has been through public-private partnership (PPP) projects, including participation in the obligatory medical insurance segment.

According to the Federal Obligatory Medical Insurance Fund, the number of private healthcare companies operating in the obligatory health insurance system continues to dramatically grow. This growth is not just in largest cities like Moscow, St. Petersburg and Kazan, but also in Russia’s regions: in Chuvashia, Penza Region and Udmurtia, several dozens of private healthcare providers were operating in the obligatory health insurance system in each of these regions in 2016. Estimates from the Deputy Prime Minister of the Russian Federation, O.Y. Golodets, state that this corresponds to 18% of the total volume of medical services provided in the obligatory health insurance market.

Despite the unfavourable macroeconomic conditions, public-private partnership (PPP) investment projects in healthcare continue to be implemented.

According to the Institute for PPP Development, the healthcare sector is one of the most active in this sphere, accounting for 10% of the total volume of private investment attracted for PPP projects. Projects to construct and operate healthcare centres that were implemented in 2014–2016 include:

— a rehabilitation facility at City Hospital No. 40 in St. Petersburg;
— a new building at the Centre for Extracorporeal Haemocorrection and Clinical Transfusiology in Samara;
— a clinical perinatal centre in Surgut.

In February 2017, at the Sochi-2017 Russian Investment Forum, a concession agreement was signed between the Government of the Leningrad Region and Special Project Company XXI Century LLC, to construct and operate Leningrad Regional Centre for Medical Rehabilitation in the town of Kommunar, Gatchina District.

Private investment into construction only is expected to reach about 2.75 billion roubles (USD 48.2 mln).

Access to financing and, consequently, the ability to forecast the long-term attractiveness of the PPP format for investors remain the key factors for successful implementation of large PPP investment projects. A reduction in the cost of borrowing in Russia, amid the low inflation conditions expected as early as 2017, will create favourable conditions for new PPP investment projects in the healthcare sector.

Changes in the number of private healthcare centers operating in the compulsory health insurance segment

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of private healthcare providers in the obligatory health insurance system</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td>1,333</td>
</tr>
<tr>
<td>2014</td>
<td>1,840</td>
</tr>
<tr>
<td>2015</td>
<td>1,943</td>
</tr>
<tr>
<td>2016</td>
<td>2,540</td>
</tr>
</tbody>
</table>

Share of the total number of healthcare providers in the obligatory health insurance segment, %

16.2 21.5 22.4 29

Sources: the Federal Obligatory Medical Insurance Fund, KPMG analysis


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