BEST'S MARKET SEGMENT REPORT

Our Insight, Your Advantage®

November 24, 2025

Market Segment Outlook: US Health Insurance

The outlook for the US health insurance segment remains Negative, reflecting ongoing higher medical trends for Medicare Advantage and rate and acuity mismatch for Managed Medicaid

AM Best is maintaining the Negative outlook for the US health insurance industry based on the following factors:

- Continuation of higher medical trends for Medicare Advantage
- Rate and acuity mismatch for Managed Medicaid
- Increased utilization and claim cost trends in commercial business
- Elevated legislative and regulatory concerns

Despite the above-mentioned concerns, offsetting factors include the following:

- Good capitalization and liquidity
- Continued favorable net investment income

Increased utilization, medical costs, and morbidity are being reported across multiple lines of business over a wide range of care. AM Best notes operating margins remain under heavy pressure in government programs, while margins have narrowed significantly in the commercial market.

Increased Medical Trend

The US health insurance industry is experiencing a broad-based increase in medical expenditures driven by higher utilization of specialty drugs, physician visits, and medical services; a greater number of inpatient admissions and emergency room visits; a rising number of behavioral health claims and an increase in the coding intensity of medical services, reflecting higher member acuity.

While there are some slight differences by line of business, most segments are experiencing an elevation of medical trends. The trends appear to have accelerated in late 2024, with underwriting earnings dropping materially in the fourth quarter. And while the industry entered 2025 with higher-than-expected medical and pharmacy utilization, the first quarter was also negatively impacted by elevated respiratory claims due to flu, COVID, and pneumonia.

The Medicare Segment Remains Challenged

Medicare Advantage (MA) plans are experiencing pressure from all sides: an increase in utilization trends and provider costs; higher morbidity from certain members; changes to the risk-adjustment payment model by the Centers for Medicare & Medicaid Services (CMS); as well as lower Star Ratings across the industry.

The elevated utilization for MA began in 2023 and has persisted longer than expected. With the aging of the US population, more people are aging into the Medicare program than ever before, many of whom delayed care until eligible for Medicare to receive enhanced benefits and potentially lower out-of-pocket costs. Moreover, the number of available MA plans declined in

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2025-157

2025 as some insurers exited certain geographies or left the market. These exits were mainly from plans that were reporting unfavorable results. Many of the members from these plans were not engaged in medical management programs and were sicker than a typical seasoned MA member. This has resulted in lower risk adjustment scores for some new members than an insurer would have typically received based upon the actual health status. Over time, as insurers gather data on the health risk of new members, the risk adjustment scores for these members should be adjusted to reflect the actual health status. Additionally, the number of available MA plans will continue to decline for 2026 which could again result in lower risk adjustment scores for new members as individuals will need to find a new plan.

AM Best notes there has been a steady decline in Star Ratings for MA plans. Only plans with 4-Star Ratings or higher receive the Star Ratings bonus payments from CMS, which is an additional 5%. CMS stipulates that the Star bonus payments must be used to benefit members in the form of lower premiums or additional benefits, which can provide a significant competitive advantage to MA plans. The average Star Rating has declined annually since the 2023 calendar year. Roughly 40% of MA plans were rated 4 Stars or higher for 2026, compared to over two-thirds in 2023.

Furthermore, CMS has been phasing in a new risk adjustment model to determine Medicare capitation reimbursement. This model, known as V28, is replacing the previous V24 model. This new methodology is being implemented over a three-year phase-in period which started in 2024. The 2025 calculation is based on two-thirds of the new model and one-third of the old method, and 2026 will be based entirely on the new V28 methodology. V28 is projected to lower the calendar year 2025 risk adjustment reimbursement payment by 2.45%, according to CMS, due to a material decline in available claims codes.

AM Best notes that the CMS rate increase to health insurers for 2026 is better than recent years and is more reflective of current trends seen through 2024. However, the pressure on MA margins will likely persist as utilization and medical trends have remained elevated.

Discernible trends in the senior population are not unique to MA. Medicare Supplement plans also observing similar elevated utilization trends and increased medical costs, especially from members who have recently aged into the program. Profitability in Medicare Supplement is being pressured, although to a lesser extent than MA.

Rate Mismatch Impacting Managed Medicaid

Medicaid plans have had a rough couple of years. Once the Public Health Emergency (PHE) expired and eligibility redeterminations began, plans saw enrollment drop significantly. Under the PHE, states were unable to disenroll members from Medicaid, so this facilitated an elevated Medicaid enrollment. Medicaid enrollment has declined by roughly 15 million members through January 2025 since the month before redeterminations started, March 2023. Individuals who were disenrolled tended to be healthier members, some of whom did not use Medicaid benefits since they had coverage elsewhere. Insurers were prepared for and expected the eventual disenrollment of many of these members. Insurers anticipated that over the course of 2025, they would receive rate increases that would match the acuity of the current population. The rate increases from states for managed Medicaid have been as expected by many carriers. However, a greater portion of current enrollees have higher morbidity correlating to higher medical utilization and costs than were expected. Additionally, Medicaid members are using behavioral health services at a much higher rate than in the past. Compounding these issues is the increased medical trend, which is being seen broadly across all health segments. Given the increased acuity and medical cost trends, the return to profitability for the Managed

Medicaid segment may take longer than expected and not correct until later in 2026, or possibly into 2027, as most contracts renew in January or July.

Medicaid also faces regulatory challenges in the upcoming years. The One Big Beautiful Bill, which was passed July 4, 2025, includes large funding cuts to Medicaid, including adding work requirements for certain eligible individuals and increasing the frequency of eligibility redetermination. While the work requirements must be implemented no later than the end of 2026, most of the other portions of the bill take effect in 2027 or beyond. The combined impacts of all provisions of the bill are projected by the Congressional Budget Office (CBO) to reduce federal and state spending for Medicaid programs by over $900 billion over the next decade, reduce the number of individuals covered by Medicaid, and increase the number of uninsured by 10 million. The major source of the savings is thought to be from the institution of work requirements for individuals eligible under Medicaid expansion, which was implemented as part of the Affordable Care Act (ACA).

Commercial Group Earnings Deterioration

The commercial group (employer group) business has historically been a dominant driver of earnings for health insurers with more consistent performance than other segments. Historically the earnings from commercial group business has offset weaker earnings in other lines of business, particularly from MA and Managed Medicaid, which are lower-margin segments. Earnings in the commercial group segment declined significantly in 2024. The weakening of results for this segment has continued into 2025, with earnings being impacted by higher utilization and rising medical and pharmacy costs mirroring most trends previously seen in Medicare and Managed Medicaid. Additionally, many health insurers saw a significant increase in the usage of GLP-1s. This class of drugs has experienced a rapid rise in both the number of approved uses and the members being prescribed the drug. AM Best notes that a number of insurers and employers have changed the coverage for GLP-1s in 2025 and are only covering this class of drugs for uses other than only for weight loss.

Given the higher medical trends, rate increases at renewal are expected to be material and could drive enrollment losses, shift more costs to the employee, whether it be via higher premiums or out-of-pocket costs, or convert from fully insured to self-funded, especially in small group business, which are more price sensitive. Additionally, increased utilization, severity, and higher claim amounts could negatively impact stop-loss carriers as more self-funded accounts may reach retention maximums and/or aggregates on medical expenditures.

Individual Business Shows Material Weakening of Earnings

The individual ACA marketplace business has reported good profitability overall for the past few years, with underwriting income outpacing commercial group. However, the trends have turned in 2025, with plans experiencing sharp increases in utilization and medical costs that are negatively impacting earnings. A deterioration in risk pools—with higher morbidity members—occurred during the 2025 open enrollment period driven by a pickup of members disenrolled from Medicaid due to the end of the PHE. Plans are seeing utilization patterns similar to Medicaid for these members with greater utilization of the emergency room and behavioral health services. Furthermore, several insurers have noted an increase in the overall morbidity of the individual ACA enrollment, which is putting further pressure on earnings from this segment.

Since the introduction of the enhanced subsidies under the American Rescue Plan Act in 2021 and extended as part of the Inflation Reduction Act passed in 2022, individual ACA Marketplace enrollment has more than doubled. Should the enhanced subsidies expire at the end of 2025, it is expected to severely impact ACA marketplace enrollment, as many individuals may no longer be

able to afford coverage. Rate increases have been generally higher compared to recent years, driven by the increased medical costs and utilization of high-cost drugs in addition to the expiration of the enhanced subsidies. Furthermore, the expiration of the enhanced subsidies could increase out-of-pocket premiums for affected individuals by up to 75%. Insurers are expecting that this will drive high enrollment losses, especially among healthier individuals. Some of the current year's increased utilization could be from individuals who may not be able to afford the rate increases and anticipate dropping coverage for 2026.

The One Big Beautiful Bill, passed in July 2025, as well as the funding bill to end the government shutdown, which was passed in November 2025, did not address continuing the enhanced subsidies. The 2026 renewal notices have been sent out which reflect the higher premiums for the expiration of the enhanced subsidies. AM Best anticipates that, given the expectation that the enhanced subsidies will end this year, the experience in this segment will worsen in the fourth quarter of 2025 as individuals seek medical care before year-end. Additionally, the challenges in this market have already resulted in some plans exiting the ACA marketplace in 2026, either entirely or in select states. Furthermore, there could be additional exits in 2027 and beyond if insurers are not able to adequately price for the risk.

Risk-Adjusted Capitalization, Liquidity, and Investment Performance

Despite these headwinds, US health insurers maintain more than adequate risk-adjusted capital levels. Favorable earnings over the past five years have driven capital growth, which has largely kept pace with premium revenue increases. This trend may be pressured by the expectation of declining operating earnings for the full years 2025 and 2026. Although AM Best notes that membership declines could offset some of this pressure, especially in 2026.

Health insurers have continued to maintain conservative investment portfolios, which are primarily comprised of investment grade fixed income and cash and cash equivalents with a relatively short duration of about six years. Equity and Schedule BA assets have remained fairly level over the past five years. Through 2024, health insurers maintained more than adequate liquidity driven mostly by positive operating cash flow, high cash balances, and most insurers have access to additional sources of liquidity if needed.

Growth in invested assets along with improved yield on fixed income securities and favorable equity market performance have delivered solid net investment income for health insurers, partially offsetting underwriting income pressure. It is expected that investment income will remain a meaningful contributor to net earnings for the full years 2025 and 2026.

Corrective Action

Despite near-term headwinds, insurers are actively pursuing initiatives to restore their long-term operating performance. Pricing actions and plan design changes are being implemented for 2026 to reflect the increased medical trends. Plans are evaluating their participation in certain market segments and/or geographies. Market exits for certain products will increase for 2026 as insurers focus on improving operating performance. Provider pricing will remain a focus with continued emphasis on value-based care and strategic provider partnerships. Health plans are looking to care management to address increased member morbidity and aid in managing the health of members. Insurers continue to review their administrative cost structure, and the adoption of automation and AI could drive operational efficiencies.

AM Best expects that operating performance for the US health insurance industry will be pressured for 2025. AM Best expects operating performance to improve in 2026, but pressures may persist into 2027, as it may take several pricing cycles to fully address the issues facing the industry.

GUIDE TO BEST'S MARKET SEGMENT OUTLOOKS

Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months. Typical factors we would consider include current and forecast economic conditions; the regulatory environment and potential changes; emerging product developments; and competitive issues that could impact the success of these companies.

A Best's Market Segment Outlook can be Positive, Negative, or Stable.

Best's Market Segment Outlook	
Positive	A Positive market segment outlook indicates that AM Best expects market trends to have a positive influence on companies operating in the market over the next 12 months. However, a Positive outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Positive.
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We update our market segment outlooks annually but may revisit them at any time during the year if regulatory, financial, or market conditions warrant.

Published by AM Best

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Version 011624