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Headline: Why ElderShield is not bad for the young

Why ElderShield is not bad for the young

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For The Straits Times

The proposal by the ElderShield Review Committee in January to make the policy mandatory is raising eyebrows, especially among the younger generation who not only share a disdain towards the name but also detest mandatory spending that cuts their pay cheque.

Many wonder why there is a need for such disability insurance in the first place. And if there is such a need, why does ElderShield start at such a young age? And how does this public insurance policy differ from the private ones? To address these concerns of the young, we have to start with the basics.

Insurance is about managing risks. There are many risks in life: health, disability, violent accidents, just to name a few. The risk of suffering from ill health at a later stage in life is higher than many of us would expect.

According to data compiled by the Centre for Research on the Economics of Ageing (CREA), where we do our research, among Singapore's elderly aged 50 to 70, 58 per cent suffer at least one chronic condition and 10 per cent have more than two conditions.

Worse, it is common for chronic conditions such as diabetes and strokes to cause disability. Among individuals with diabetes, 10 per cent could not perform at least one activity of daily living (ADL). After having a stroke, 14 per cent of individuals fail to perform at least three ADLs.

Acknowledging the risks in life, one faces three choices:

- Prepare for rainy days by saving and investing;
- Buy some sort of insurance;
- Do nothing and hope for the best.

Option 3 is obviously not feasible because without any financial assurance, individuals are left with severe vulnerabilities later in life.

Contrary to popular belief, option 1 is inadequate and inefficient.

In the event of a health shock, high medical fees can quickly consume savings and force one to reduce consumption and eventually take on debt. In fact, medical debt is already the No. 1 cause for household bankruptcy in the United States.

When misfortune strikes, with one becoming disabled or plagued by chronic conditions, medical expenses include hospital fees, long-term care costs, medicine fees and other miscellaneous services. The sum involved can get enormous, especially in the last few years of life prior to death.

A British study has found that in the last year before death, US medical spending averages US$80,000 (S$105,000). Without insurance coverage, a large sum of money has to be put aside to pay for medical expenses which could have been used for a more enjoyable retirement.

Hence, the most logical solution is joining an insurance scheme – option 2. This is especially true for young people, when premiums are at their lowest. But this is not a popular choice because people often underestimate future risks.

The young tend to prioritise spending for satisfaction today, instead of saving for the long term. Apart from employment-based insurance, few young people would voluntarily buy supplementary insurance products. This aligns with global trends and is understandable. Hence, even with an ElderShield plan that costs under $20 per month, arguably a sum that will not affect lifestyles much, there is some reluctance among young people to take this up.

But if it is so necessary to have insurance, why can't people just purchase individual private plans?

Private plans have essential flaws where the higher the perceived risk, the higher the premium. It is unrealistic that everyone has the same health condition and age upon buying an insurance plan. Therefore, the premium required for each individual varies, where the healthy and young pay a lower premium and may not need payouts until much later in life. The not so healthy 65-year-olds pay a higher premium or are denied insurance due to pre-existing conditions.

This raises the puzzle of insurance: adverse selection, where people most in need of insurance are least able to afford the higher premiums. Mandatory public insurance schemes can overcome this hazard by creating a large enough group of people to pool the risk, and hence lowering the premiums for all.

To be sure, ElderShield is a fairly basic insurance plan that provides coverage for those who might not otherwise qualify or be able to afford such long-term care. By making it mandatory for younger Singaporeans, it also pushes the young to put aside a small pool of money for a rainy day, without affecting their current consumption patterns.

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