Fitch: Potential Medicaid Cuts Could Threaten Not-for-Profit Hospital Margins

Fitch Ratings-Chicago/Austin/New York-04 March 2025: Major cuts to Medicaid would negatively affect U.S. not-for-profit (NFP) hospital operating margins and revenues, Fitch Ratings says. Slower revenue growth or a revenue decline leading to sustained cash flow reduction could pressure ratings and potentially the sector outlook.

The House's recently passed budget proposal calls for $1.5 trillion-$3.0 trillion in spending cuts over the next decade. It includes a directive to the Energy and Commerce Committee to reduce spending by $880 billion over the next 10 years. The Senate will likely propose changes to the House plan, which would require another vote on a final budget resolution before work on budget details can commence.

Although the House plan does not mention specific programs, Medicaid and Medicare are the largest under the Energy and Commerce Committee's purview. Achieving the budget cuts would be difficult without changing Medicaid eligibility or Medicaid funding. It is uncertain what Medicaid changes, if any, will be in the final budget bill and how they would affect funding and enrollment. Approximately one in five Americans are covered by Medicaid.

A decrease in Medicaid reimbursement and/or an increase in uninsured care would hinder hospitals' nascent financial recovery from weak sector-wide post-pandemic performance due to higher labor costs and elevated inflation. Median operating margins, which are lower than pre-pandemic levels, are improving along with revenue growth due to increased patient volumes. However, lower revenues and higher unreimbursed expenses from more self-pay patients could reverse recent improvements. This is particularly true for hospitals with a higher share of Medicaid patients, which inherently have thinner margins.

NFP hospitals have limited ability to cut services, given operating constraints such as the obligation to serve all needing medical care. They also cannot pass through costs, as reimbursement rates are contracted with public and private insurance providers for set timeframes. Government reimbursement through Medicare and Medicaid programs are generally set annually by the Centers for Medicare & Medicaid Services without negotiation.

Payor mix is an important component in our assessment of a hospital or healthcare system's revenue defensibility, a key driver of ratings under our Not-for-Profit Hospitals and Health Systems Ratings Criteria. Greater exposure to self-pay and Medicaid reimbursement reduces a hospital provider's capacity to recover its operating costs from other payor sources. Safety-net hospitals, with combined self-pay and Medicaid payers of more than 30% of gross revenues, have 'very weak' revenue defensibility. Providers with 25%-30% exposure have 'weak' revenue defensibility assessments.

The effects of any Medicaid cuts on NFP hospitals would depend somewhat on state Medicaid policies and other healthcare options. The Federal Medical Assistance Percentage (FMAP), the percentage of a state's Medicaid spending matched by the federal government, is generally tied to each state's wealth levels. A federal statute sets a FMAP floor of 50% for states with the highest per-capita income and a ceiling of 83%. The FMAP's significance depends on each state's total budget size and Medicaid spending, which vary based on factors like enrollee levels, composition, and reimbursement rates.

States may choose to allocate more of their own resources to Medicaid funding to mitigate the effects of federal cuts, or reduce benefits, eligibility, or provider payment rates. California, New York, Texas, Pennsylvania and Ohio, the states with the largest populations, receive the most federal Medicaid funding, according to KFF.