April 2025

Navigating potential policy changes to government-sponsored health insurance programs

Reviewing enterprise risk and liquidity for healthcare organizations

Introduction

Medicare and Medicaid were enacted as part of the Social Security Amendments of 1965 and are managed under the umbrella of the Centers for Medicare & Medicaid Services (CMS). Nonprofit hospital systems derive approximately 45% of their revenues from these programs, roughly 35.6% from Medicare and 9.4% from Medicaid based on payer mix data.

In light of mounting federal deficits and the policy priorities of the new administration, there is a renewed focus on adjusting federal finances through a combination of tariffs, tax policy and spending cuts. While much of the discussion revolves around trade and tax changes, this paper focuses on the potential spending cuts within Medicare and Medicaid, the two largest federal programs that have had the most impact on healthcare funding for six decades.

These proposed policy changes are part of a House budget resolution that directs the Energy and Commerce Committee to find over $800 billion in savings over the next decade. While the resolution does not explicitly mention Medicaid or Medicare cuts, achieving this level of savings would likely require significant reductions to these programs. The potential cuts to Centers for Medicare & Medicaid Services (CMS) could have significant implications for healthcare providers, state budgets and financial planning within the healthcare system.

Such funding reductions could reverse the modest financial recovery seen in the nonprofit hospital sector following the pandemic. Hospitals already face challenges like rising operating costs and high medical utilization rates, which further compound the risks of Medicare and Medicaid cuts.

This paper explores those potential impacts and outlines strategies for organizations to manage the risks posed by these changes.

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Medicare and Medicaid areas of focus impacting healthcare systems

Medicare: Site-neutral payments and reimbursement adjustments

Medicare, a federal program primarily serving individuals aged 65 and older, is under review for potential policy adjustments. A few areas that have recently been discussed include site-neutral payments and modifications to Medicare reimbursement rates.

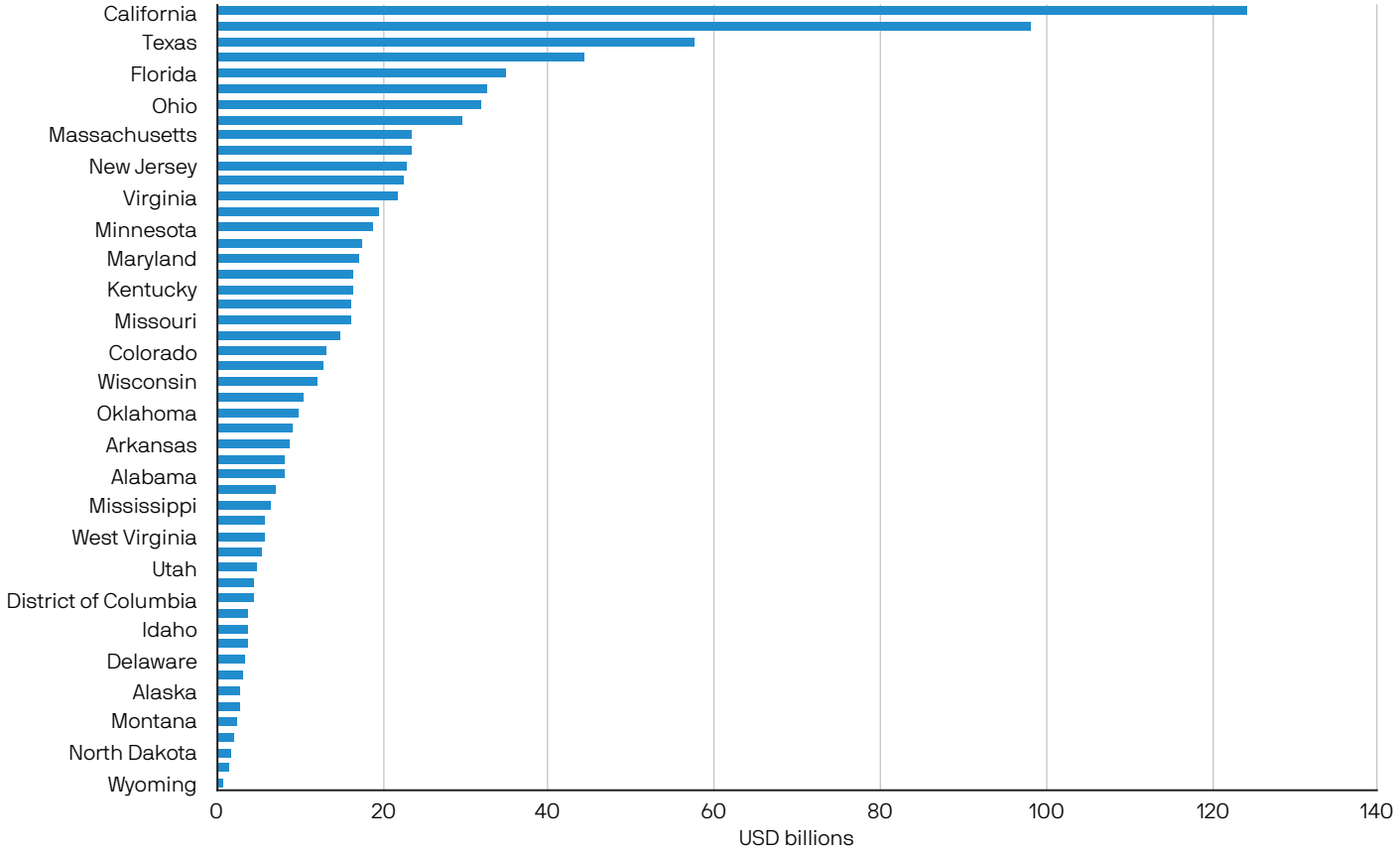
- **Site-neutral payments:** The government aims to standardize reimbursement rates between hospital outpatient departments (HOPDs) and independent physician offices, eliminating financial disparities. For example, an MRI performed at a hospital outpatient department may currently be reimbursed at $1,200, whereas the same MRI in a physician's office might receive only $800. Under site-neutral policies, both would be reimbursed at the lower rate, reducing hospital revenue.
- **Reimbursement rate changes:** There is additional focus on further reducing Medicare reimbursement rates. Any new adjustments to current Medicare reimbursements could further strain hospital finances, particularly in underserved and rural areas, where hospitals rely on higher outpatient reimbursement rates to subsidize operations and maintain staffing levels.

Medicaid: Federal Medical Assistance Percentage (FMAP) adjustments and per-capita caps

Medicaid, a joint federal and state program providing healthcare coverage to low-income individuals, is also facing potential changes:

- **Federal Match Rates (FMAP) adjustments:** Federal contributions to Medicaid vary by state based on per-capita income. States with high Medicaid enrollments and lower per-capita incomes—such as West Virginia, Kentucky, and Mississippi—would be more heavily impacted by FMAP reductions, forcing them to either raise state funding or cut services. Conversely, higher-income states with lower Medicaid reliance—like Massachusetts or Connecticut—would see relatively smaller budget shortfalls.
- The 41 states that extended Medicaid eligibility to individuals under 65 will face increased pressure to fill a larger funding gap at the state level if federal funding under the Affordable Care Act is decreased, as they have relied on this additional funding to support their expanded programs.
- **Per-capita caps:** Proposed funding caps would limit federal Medicaid contributions per enrollee, affecting states with large, aging or high-need populations. This could lead to eligibility restrictions, benefit reductions or reimbursement cuts to providers, disproportionately impacting healthcare systems reliant on Medicaid funding.

Exhibit 1: Total Medicaid spending , fiscal year 2023



Source: Estimates based on data downloaded from CMS (Form 64); data as of September 2024.

Notes: Total Medicaid expenditures do not include administrative costs, accounting adjustments, or the U.S. Territories. Total Medicaid spending including these additional items was $860 billion in FY 2023.

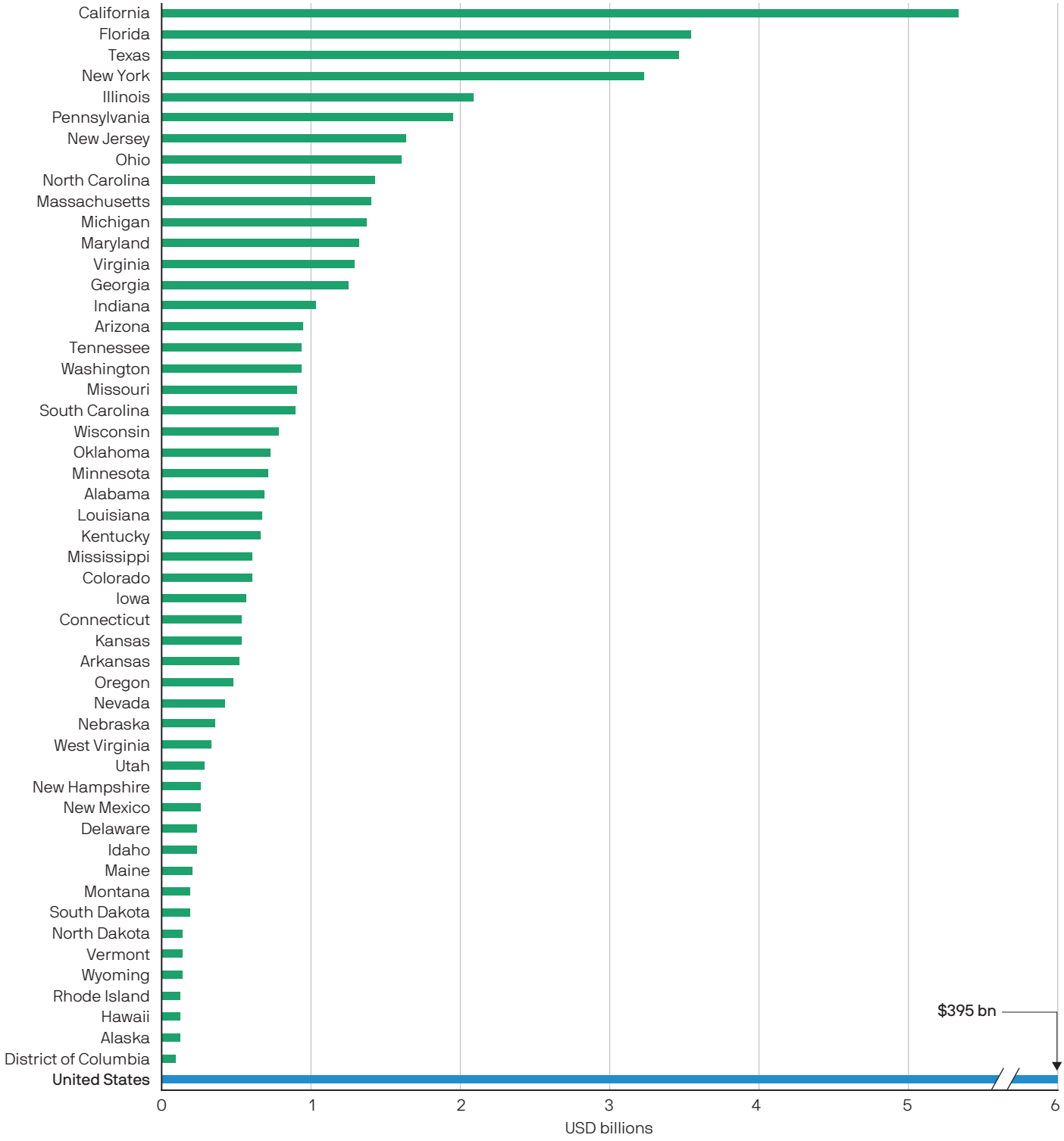
Definitions: Federal Fiscal Year—Unless otherwise noted, years preceded by "FY" refer to the Federal Fiscal Year, which runs from October 1 through September 30. FY 2023—refers to the period from October 1, 2022 through September 30, 2023.

Potential impact on revenues and balance sheets

The proposed changes to Medicare and Medicaid could significantly impact hospital revenues, particularly for those with substantial outpatient services or high Medicaid patient volumes. Lower reimbursement rates and delayed payments could create liquidity challenges, forcing hospitals to reconsider capital expenditures, staffing and investment in new technologies.

Additionally, a state-by-state analysis of Medicare spending highlights where the largest cuts are likely to occur. **Exhibit 2** ranks Medicare spending by state (highest to lowest), along with estimated 10-year cuts based on a 2% reduction scenario, and provides insight into which regions could experience the most significant funding reductions. This data reinforces the importance of financial planning for healthcare providers operating in high-reimbursement states.

Exhibit 2: Total Medicare spending , fiscal year 2023



Source: Centers for Medicare & Medicaid Services, Office of Enterprise Data and Analytics, Chronic Conditions Data Warehouse; data as of September 30, 2023.

Strategic considerations for healthcare systems

To navigate the potential impacts of Medicare and Medicaid policy changes, healthcare systems must adopt a proactive approach to enterprise risk management. This includes assessing cash flow risk, reimbursement timing and investment strategy to maintain financial stability.

Investment strategy: alternatives to moving into cash

Given the risk of funding shortfalls, healthcare organizations must consider more effective liquidity management strategies than simply moving into cash. While cash preserves flexibility, it may not generate sufficient returns to offset revenue declines. Instead, short-term, high-quality corporate and securitized fixed-income investments can provide an additional 25 to 50 basis points (bps) of return over cash while maintaining liquidity.

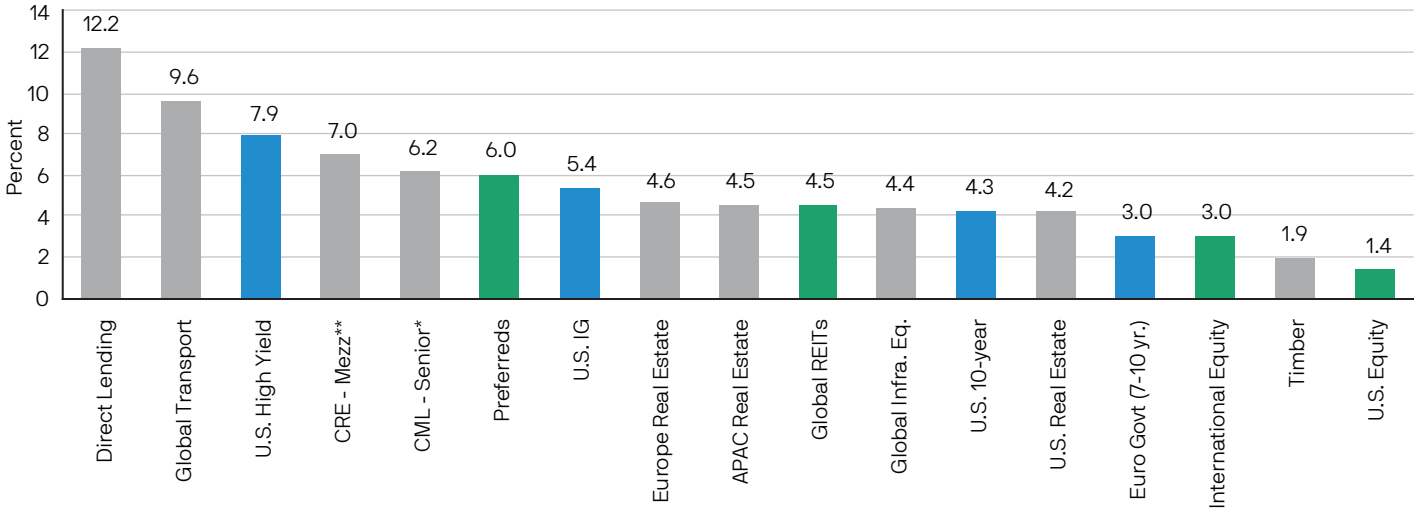
For organizations with potential cash needs over the next three to seven years, but with uncertain timing, a medium-term liquidity pool focused on stable income-producing alternatives could be an optimal approach. This portfolio could include:

- **Real assets:** Investments in core real estate, infrastructure and transportation provide low volatility and stable income streams.
- **Private credit:** Private credit strategies can generate attractive risk-adjusted returns with consistent cash flow, meeting the dual objectives of stable returns and an income-producing portfolio.

In nonprofit healthcare systems, liquidity and investment risk are two of the most significant challenges, with liquidity serving as a critical factor in shaping investment strategies. Generally, the greater an organization's liquidity and financial strength, the higher its capacity for risk tolerance. Conversely, limited liquidity necessitates a more conservative investment approach. Establishing a realistic investment risk tolerance involves understanding and planning for the volatility and potential drawdowns a system can endure. This is intrinsically linked to liquidity, balance sheet health and the viability of the operating outlook.

By taking a structured approach to liquidity and investment planning, healthcare organizations can mitigate the risks associated with Medicare and Medicaid cuts, ensuring operational stability and the continued delivery of quality care to patients (**Exhibit 3,** next page).

Exhibit 3: Current yields by asset class



Source: BAML, Bloomberg, Clarkson, Cliffwater, Drewry Maritime Consultants, Federal Reserve, FTSE, MSCI, NCREIF, FactSet, Wells Fargo, J.P. Morgan Asset Management.

*CML is commercial mortgage loans.

**CRE – Mezz is mezzanine commercial real estate debt. Equities and fixed income yields are as of February 28, 2025. Alternative yields are as of September 30, 2024, except Timber, which is as of December 31, 2024; CRE- Mezz, which is as of February 28, 2025; and CML – Senior, which is as of December 31, 2024. CML – Senior: Market-capitalization weighted average for all mortgages in the Gilberto-Levy Commercial Mortgage Index. Mezzanine commercial mortgage loans yield is derived from a J.P. Morgan Survey and U.S. Treasuries of a similar duration. Global Transport: Levered yields for transport assets calculated as the difference between charter rates (rental income), operating expenses, debt amortization and interest expenses, as a percentage of equity value, and are based on a historical 15-year average. Yields for each of the sub-vessel types are calculated and respective weightings are applied to arrive at the current levered yields for Global Transportation; Preferreds: BAML Hybrid Preferred Securities; Direct Lending: Cliffwater Direct Lending Index; U.S. High Yield: Bloomberg U.S. Aggregate Corporate High Yield; Global Infrastructure: MSCI Global Private Infrastructure Asset Index; Global REITs: FTSE NAREIT Global REITs; International Equity: MSCI AC World ex-U.S.; U.S. 10-year: 10-year U.S. Treasury yield; U.S. Equity: MSCI USA, Europe Real Estate: Market weighted-avg. of MSCI Global Property Fund Indices—U.K. & Cont. Europe; U.S. and Asia Pacific (APAC) core real estate: MSCI Global Property Fund Index . Euro Govt. (7–10 yr.): Bloomberg Euro Aggregate Government—Treasury (7–10Y); Timber: NCREIF Timberland Index (U.S.)—EBITDA Return. Past performance is not a reliable indicator of current and future results.

Conclusion

While the actual magnitude of cuts and changes to Medicare and Medicaid is still unknown, healthcare organizations must prepare for potential financial impacts. By implementing a strategic enterprise risk approach—leveraging higher-yielding, short- and medium-term investments instead of simply moving into cash—organizations can mitigate revenue volatility, maintain liquidity and continue delivering high-quality care. Thoughtful financial planning will be critical to navigating these changes and maintaining long-term stability in an evolving healthcare landscape.

Next steps

Please reach out to your J.P. Morgan Asset Management team with any questions or to further discuss in detail.

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