Medicaid Cuts: Measuring Potential Downstream Credit Impact on State and Hospital Sectors

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Executive Summary

- The recent passage of the House Ways and Means Committee tax reconciliation bill has preserved the tax exemption for municipal bonds and provided some certainty for government issuers planning long-term capital projects.
- We examine the potential risks stemming from the proposed federal cuts to Medicaid funding and its potential impact for state and healthcare credit, particularly in states that expanded Medicaid under the Affordable Care Act (ACA).

Medicaid and the Trump Administration Tax Bill

While several unknowns still exist for municipal issuers going into the second half of 2025, the recent passage of the House Ways and Means Committee tax reconciliation bill preserving the tax exemption for municipal bonds (Munis) has provided one element of certainty. The passage allows government issuers to potentially better plan capital funding needs, especially for longer term capital projects with less concern over the prospect for higher costs of capital.

Despite this, some degree of uncertainty remains surrounding the final form of the tax bill that could more directly impact state and healthcare credit, specifically as it relates to the contemplated cuts to federal dollars directed to states to help pay for Medicaid Expansion opted into under the ACA. Federal Medicaid funding, a sizeable budget line item, is under consideration for cuts to help pay for the extension of The Tax Cuts and Jobs Act (TCJA) of 2017 enacted under the first Trump Administration and is set to expire at the end of 2025.

The size of the potential federal cuts remains unknown as the tax bill is actively being marked-up by the Senate, and the mechanism through which federal savings may be achieved, whether through eligibility rules modification or reduction in Federal Medical Assistance Percentage (FMAP) is still unclear. Ultimately, any reduction in federal funds shifts more of the cost burden to state governments and municipal obligors who are downstream beneficiaries of state funding.

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[1] Medicaid Expansion Spending www.kff.org (accessed (06/11/2025)
[2] Federal spending for the state expansion group totaled $158.3bn in FY2023. State and Federal spending (traditional Medicaid and expansion program) totaled $863.8 bn in FY2023.

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Credit Impact of Medicaid Cuts on Municipals

Potential federal cuts to Medicaid may have downstream credit implications more directly on state finances and hospital operations, but that would depend on the final form of the tax bill. A state's financial resilience and short-term budgetary flexibility will be a factor in how well a state can manage this disruption. A hospital's fundamentals—including its structure (single site or integrated system), geographic diversity, specialty offerings, payor mix (reliance on Medicaid reimbursements), and financial wherewithal (cash position and healthy operating margin)—are factors that may determine a credit's ability to cushion policy change.

States State credit generally is healthy despite the challenges of slowing overall economic conditions, inter-state migration, aging population, inflation, and tariffs. The 50-state median rainy day fund balance reached 49.1 days or 13.5% of spending in FY2024, a rising trend that started in 2010 after the Great Recession, from a low of 6.0 days or 1.6% of spending. Total fund balances, however, have dropped to a 50-state median of 103.7 days or 28.4% of spending in FY2024, from a peak of 144.2 days or 39.5% of spending in FY2022. These drawdowns of ending balances may be attributable to one or more factors, including growing expenditures, slowing revenue, debt repayment or non-recuring funding. A lower ending balance, regardless of its use, means reduced fiscal flexibility.

Hospitals Healthcare credit has emerged from the official end of the Covid pandemic, with some degree of stabilization, while still uneven across the sector. From mandated shutdowns (lower admissions) to higher inflation, borrowers' ability to cut costs through downsizing contract labor, renegotiating vendor contracts, and restructuring debt, have contributed to a return to positive margins. As of April 2025, cumulative operating margin reached 3.3% in contrast to 2022, which according to Kaufman Hall was the worst financial year since the start of the pandemic, with half of hospitals ending the year with negative margins (2022 ended with a median operating margin of 0.2%).

To illustrate the impact of potential federal cuts to Medicaid, we examined the top 15 states in debt outstanding (which account for approximately 79.0% of total state debt outstanding) and assumed that both states with and without trigger laws would temporarily fully fund their respective federal shares of Medicaid Expansion costs for two years as a stopgap measure, while state legislatures work towards longer-term, sustainable solutions. Medicaid expansion is expensive relative to state budgets, even with the existing 90.0% federal match rate in place. Simply funding the full cost of the federal share on a multi-year go-forward basis may cause fiscal strain. There could be instances where certain states, with both the financial flexibility and legislative support, fund the expansion for a longer period.

It is also assumed that states will not pursue quick short-term savings by cutting optional benefits, raising revenue (raise existing taxes or creation of new taxes), or restrict eligibility (coverage for certain populations).

State rainy day funds are assumed to not be available for use in this case. The primary purpose of a rainy day fund is to address an unanticipated annual deficit to balance a budget during an economic downturn where naturally revenues drop, and expenditures rise. It is effectively a one-time source of funds that is replenished over time. Such downturns are perceived as temporary and typically last a business cycle. In contrast, a potential cut in federal funding is viewed as a more permanent and structural change to the budget. Additionally, the conditions for withdrawals and repayment vary across state constitutions.

[1] Pew Charitable Trust Fiscal 50 www.pew.org (accessed 06/11/2025)
[2] Pew Charitable Trust Fiscal 50 www.pew.org (accessed 06/11/2025)
[3] Kaufman Hall National Hospital Flash Report - April 2025 (accessed 06/11/2025) www.kaufmanhall.com
[4] Kaufman Hall National Hospital Flash Report - January 2023 (accessed 06/11/2025) www.kaufmanhall.com

Table 1: Pressure Test - Full Funding of Medicaid Expansion by States for a Period of Two Years

	LIQUIDITY		LEVERAGE		BUDGET FLEXIBILITY		TAXPAYER BURDEN
State	State Funds Own Share and Federal Share % of TGFR (p.a.)	Days Each State Could Pay for Medicaid Expansion with RDF	Incremental Medicaid Expansion Debt per Capita	Adjusted Tot. Net Direct Debt per Capita	Incremental Annual Debt Service Cost to Fixed Cost Burden as % of TGFR (p.a.)	Adjusted Fixed Cost Burden as % TGFR (p.a.)	Total Cost per Capita as % of Per Capita Personal Income
CT	17.9%	485	1,382	6,251	0.9%	24.7%	1.5%
IL	19.7%	30	1,425	3,603	1.1%	22.5%	2.1%
NJ	16.0%	21	1,131	2,859	0.8%	20.3%	1.4%
MA	15.2%	866	968	5,091	0.5%	14.1%	1.1%
MD	19.3%	295	1,190	3,592	0.9%	12.5%	1.6%
PA	23.6%	247	1,174	2,112	0.9%	9.8%	1.7%
WA	25.2%	24	2,514	4,713	1.9%	7.8%	3.1%
OR	21.1%	108	2,157	4,138	1.4%	7.3%	3.2%
CA	19.0%	263	1,587	3,532	1.0%	6.9%	2.1%
NY	20.0%	142	1,639	4,579	0.8%	6.6%	2.0%
CO	23.5%	265	976	1,695	1.1%	6.3%	1.2%
OH	20.7%	175	1,237	1,973	1.2%	5.0%	2.0%
MN	17.9%	356	1,145	2,169	0.7%	3.7%	1.6%
Median	**19.7%**	**247**	**1,237**	**3,592**	**0.9%**	**7.8%**	**1.7%**

NOTES
1 RDF: Rainy Day Fund.
2 TGFR: Total Governmental Funds.
3 Incremental fixed cost burden is the debt service on 30-year debt at 4.5% assumed to fund federal Medicaid expansion subsidy for a period of two years.
4 Incremental debt per capita related to expansion costs is assumed to be principal only and not the associated interest costs.
5 Per annum (p.a.).
6 Table ranked by Adjusted Fixed Cost Burden as % of TGFR.

Sources: Creditscope, Medicaid.gov, PTAM.

Key Findings

- **Emergency Liquidity** Rainy day funds designed to resolve short-term, one-time unanticipated budget deficits, should they be allowed by states, would only fund Medicaid Expansion costs as a "one-time measure" for less than one year at the median.

- **Debt Burden** Leverage as measured by state debt per capita would grow 84.6% at the median if funded with debt for a two-year period. Higher leverage would pressure a state's tax base and revenue sources leaving less room for debt capacity intended for other priorities.

- **Taxpayer Burden** An alternative approach of looking at the additional cost is on a per capita basis as a percent of personal income. The median burden to fund the two-year expansion cost would amount to 1.7% of per capita personal income, which could be a challenging proposition for lower income populations.

- **Hospital Exposure** Hospitals with the highest median Medicaid payor mix are in Kentucky, Louisiana, New York, California, and Hawaii, all of which are Medicaid expansion states. Hospital facilities located in states with a higher share of vulnerable populations may experience operating margin erosion, as millions could be at risk of losing access to care, which in turn would increase uncompensated care costs (including safety net and rural hospitals). Hospitals with relatively weaker fundamentals and a higher proportion of Medicaid payor mix, located in states with less budgetary flexibility and lower financial resilience, may be impacted most.

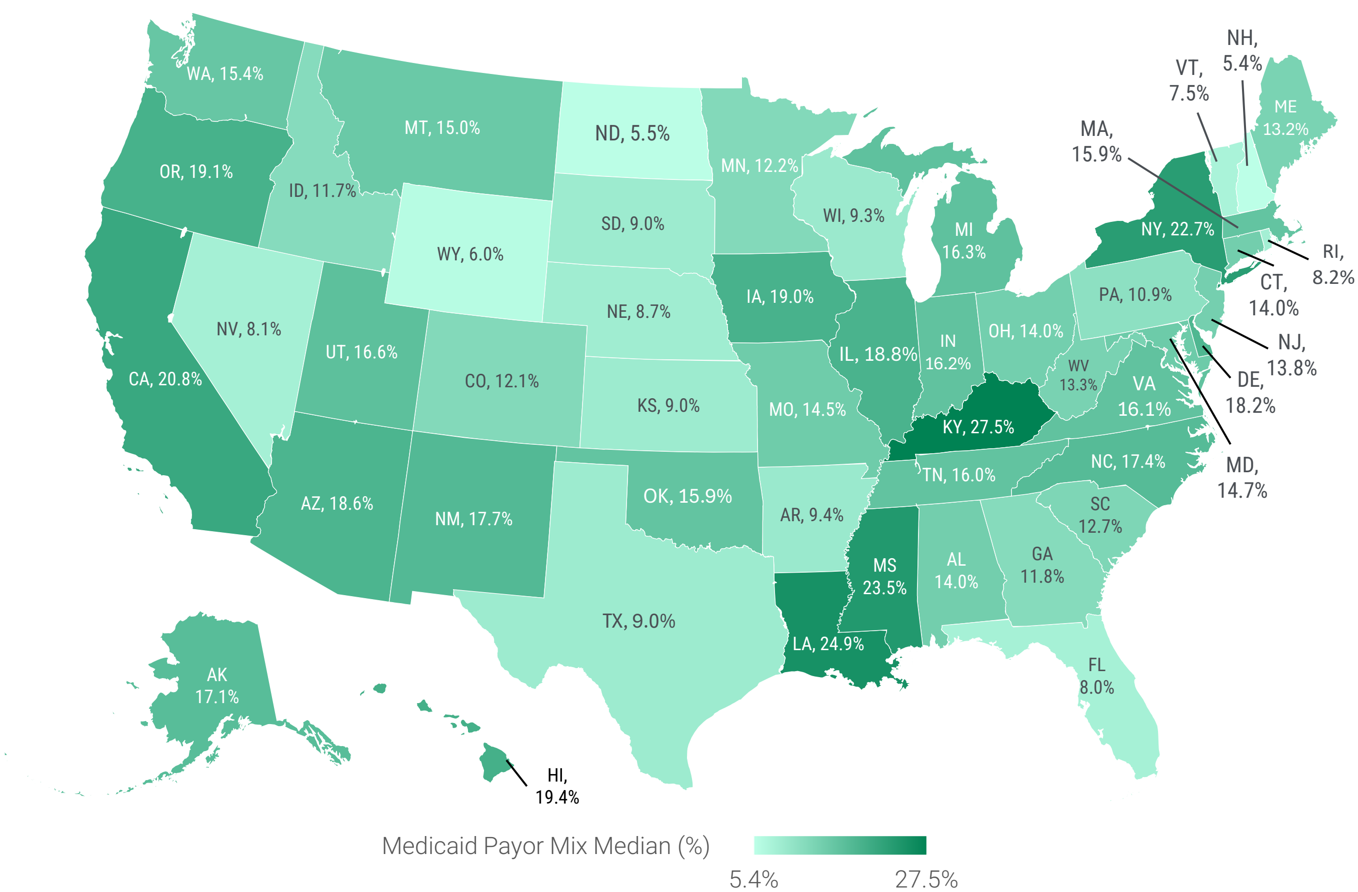
Table 2: Current State Financial Profile (pre-finalized tax bill)

		POLICY		OPERATIONS		MEASURES OF FINANCIAL FLEXIBILITY		
State	Credit Rating (SP/M/F)	Expansion State	Trigger Law?	Federal Share of Medicaid Expansion Cost % TGFR	State Tot. Medicaid Spending % TGFR	Fixed Cost Burden % TGFR	Days State Operations Can Run on RDF (GF) (p.a.)	Net Direct Debt per Capita
WA	AA+/Aaa/AA+	Yes	No	13.4%	8.4%	5.9%	5	2,199
OR	AA+/Aa1/AA+	Yes	No	10.6%	8.3%	5.9%	33	1,981
OH	AAA/Aaa/AAA	Yes	No	8.8%	10.0%	3.8%	31	736
CO	AA-/Aa2	Yes	No	8.2%	13.4%	5.2%	30	719
IL	A-/A3/A-	Yes	Yes	8.1%	10.0%	21.4%	4	2,177
CA	AA-/Aa2/AA	Yes	No	7.4%	10.2%	5.9%	43	1,945
PA	A+/Aa2/AA	Yes	No	7.1%	14.9%	8.9%	21	938
MD	AAA/Aa1/AAA	Yes	No	6.7%	11.3%	11.6%	23	2,402
CT	AA-/Aa3/AA-	Yes	No	6.6%	10.0%	23.8%	51	4,869
NY	AA+/Aa1/AA+	Yes	No	6.1%	12.7%	5.8%	21	2,940
NJ	A/A1/A+	Yes	No	6.0%	9.1%	19.5%	2	1,728
MN	AAA/Aaa/AAA	Yes	No	5.6%	11.3%	3.0%	44	1,024
MA	AA+/Aa1/AA+	Yes	No	4.0%	10.6%	13.6%	55	4,123
FL	AAA/Aaa/AAA	No	N/A	N/A	N/A	3.2%	30	181
TX	AAA/Aaa/AAA	No	N/A	N/A	N/A	6.5%	57	279
Median				**7.1%**	**10.2%**	**5.9%**	**30.5**	**1,981**

NOTES
1 RDF: Rainy Day Fund.
2 TGFR: Total Governmental Funds.
3 Median Calculated for expansion states only.
4 GF: General Fund.
5 Table ranked by Federal Share of Medicaid Expansion Cost as % of TGFR.

Sources: Current state fixed cost burden (Moody's); rainy day fund, net direct debt, personal income and population (Creditscope); Medicaid expansion cost (Medicaid.gov); trigger laws (KFF), PTAM.

Chart 1: Hospital Median Medicaid Payor Mix by State



Sources: Creditscope and PTAM.

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Glossary

Medicaid Joint federal and state program that provides health coverage to low-income individuals and families, **Payor Mix** Refers to the breakdown of a hospital's revenue sources which include Medicare/ Medicaid, commercial insurance and self-pay. **Total Fund Balance** Net resources available in a state's governmental funds at the end of a fiscal year (includes general fund and rainy-day fund). **Trigger Law** Laws in place that would automatically end Medicaid expansion or require changes if the federal match rate were to drop. Not all trigger laws would immediately end the Medicaid expansion. **Fixed cost burden** Consists of annual recurring fixed costs needed to meet long-term obligations (debt service payments, pension contributions, and retiree health care contributions [OPEB]). **Net direct debt** means total direct debt minus self-supporting debt. **Self-supporting debt** is debt with a specific revenue source pledged for its repayment. **Total Fund Balance** Net resources available in a state's governmental funds at the end of a fiscal year (includes general fund and rainy-day fund). **Total government funds revenue (TGFR)** Total governmental revenue is used for calculation of certain metrics as it gives a more comprehensive view of states financial sources and expenditures.

Risks and Other Important Considerations