How pediatric health providers should rethink their strategies

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In brief:

01 Recent actions by the Trump administration and Congress, combined with existing headwinds, are likely further to consolidate providers and reduce capacity for pediatric care.

02 Providers that leverage this moment for strategic repositioning, tough decisions, and focused growth will emerge as market leaders.

03 Strategies tailored to each organization's mission will focus on redefining the vision, exploring revenue-building opportunities, driving operational improvement and managing costs effectively.

Health systems providing care for children find themselves at the center of existing challenges and new government actions.

Recent and proposed actions by the administration and Congress have broad implications for patients, families, care teams and the economics of hospitals and health systems. Significant changes to Medicaid and research funding are already poised to have a negative impact on institutional revenue, while tariffs threaten to increase the costs of supplies and equipment.

For many years, pediatric providers have been navigating the turbulent waters of increased costs due to inflation, technology investments and shifting consumer preferences combined with a lagging reimbursement model that is not keeping pace with these factors.

The question for many is: "How long will our organization be solvent under current operations?" Although some organizations are starting from a stronger position, the answer for many will be "not long."

EXISTING HEADWINDS

Market consolidation and reductions in pediatric capacity have already started.

The nearly 20% decline in pediatric inpatient beds between 2008 and 2022, with only a 1.2% decline in the pediatric population, indicates the pediatric care landscape was stressed prior to this administration's actions.[1]

The economic model for providing pediatric care has been strained by increasing costs, lagging reimbursement and a shrinking market (see Figure 1 below).

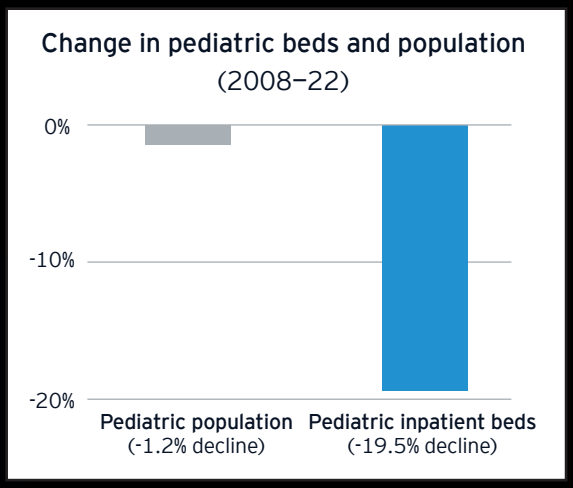

Figure 1:

Existing pediatric headwinds		Description
CONTRACTING MARKET	Declining pediatric population	The U.S. Census Bureau projects that from 2025 to 2040, the US total pediatric population and patient base will decrease by ~5%.[2]
STRESSES ON REVENUE	Shifts to ambulatory settings	Government and commercial payers are actively pushing care to ambulatory settings to lower costs. Often preferable for patients and providers, the shift to ambulatory settings represents a decrease in revenue and margin for the provider organization.
	Mental health care crisis	The limited supply of mental health providers and coverage for services has strained pediatric emergency departments (EDs). From 2007 to 2016, pediatric ED visits for mental health increased 60%[3] and from 2018 to 2021 averaged over one million visits annually, with ~60% covered by Medicaid.[4]
	Time lag on Medicaid payments	While different in each state, some providers experience a significant lag between providing care and receiving the full payment.
INCREASING COSTS	Inflation in labor and supply costs	Post-pandemic inflation across medical supplies, wages and specialty drugs is outpacing reimbursement increases. Labor shortages in some geographies and specialties are pushing salaries higher.
	Increasing technology investment	Technology has become an increasingly significant spend, including electronic medical records (EMRs), enterprise resource planning (ERP), customer relationship management (CRM), cybersecurity and artificial intelligence (AI) integration, representing hundreds of millions of dollars in investment by providers.
	Responding to consumer preferences	As newer retail and virtual models scale, providers face mounting pressure to invest in improving digital and traditional care to compete on convenience and experience.

[1] "U.S. Hospitals Lost Almost 30% of Pediatric Inpatient Capacity Over a Decade," *Children's Hospital Los Angeles website*.
[2] "2023 National Population Projections Tables: Main Series," *U.S. Census Bureau website*, www.census.gov/data/tables/2023/demo/popproj/2023-summary-tables.html.
[3] "Children's Mental Health Emergency Department Visits: 2007-2016," *National Library of Medicine website*, pubmed.ncbi.nlm.nih.gov/32393605/.
[4] "Emergency Department Visits Related to Mental Health Disorders Among Children and Adolescents: United States, 2018-2021," National Health Statistics Reports, www.cdc.gov/nchs/data/nhsr/nhsr191.pdf, October 24, 2023.

NEW HEADWINDS

Pediatric providers are also facing a wave of recent actions and potential policy changes that will negatively affect financial viability, further exacerbating the impact of existing headwinds (see Figure 2 below).

Figure 2:
Administration and congressional headwinds

Recent and proposed actions		Description
RECENT LEGISLATION	Changes to Medicaid funding for states	■ Work requirements will likely negatively affect coverage for children as well as adults. ■ For every 100 adults who lose Medicaid coverage, it is estimated that ~5 children also lose coverage; this could affect 480,000 to 914,000 children nationally.[5] ■ The nonpartisan Congressional Budget Office estimates that recent legislation will reduce Medicaid funding by ~$1 trillion and loss of coverage for ~11.8 million people over the next 10 years.[6]
EXECUTIVE ACTIONS	Research funding	While legal challenges are ongoing, executive orders have included: ■ Bans on federal grants that have impacted research related to women's health, minority populations and LGBTQ+ populations. ■ National Institutes of Health (NIH) and Centers for Disease Control and Prevention (CDC) funding freezes and staffing cuts ■ Caps on indirect costs for grants at 15%, which would reduce indirect payments by ~50%
	Tarriff increases and uncertainty	■ Medical supply chains may realize price hikes and volatility due to ongoing tariff uncertainty. ■ Nearly 70% of US-marketed devices are manufactured outside of the US, and most protective gear worn by health care workers is made in China.[7, 8] ■ Pediatric providers will absorb higher costs they cannot pass onto consumers or insurers.
FY26 PROPOSED BUDGET IMPACT	Research and education funding cuts	The president's FY26 budget proposal includes: ■ 40% cuts to NIH funding (~$19 billion in cuts) and consolidation of institutes that could reduce pediatric research funding by ~$700 million in FY26[9] ■ Eliminating the Children's Hospitals Graduate Medical Education program, which awarded $367 million in funding to 59 stand-alone children's hospitals in FY24[10]
PROPOSED REGULATORY UPDATES	Updates to 340B Drug Pricing Program	■ 340B provides margin to many hospitals, used to offset un- and under-reimbursed services. ■ A recent executive order establishes legal grounds for the administration to execute 340B reimbursement rate reductions.
	Site-neutral payment expansion	■ The Centers for Medicare & Medicaid Services (CMS) has proposed expansions to site-neutral payments and elimination of the "in-patient only" list to move care to lower-cost settings. ■ Commercial payers are likely to continue a similar push to ambulatory settings.
NON-FINANCIAL DISRUPTORS	DEI rollback	■ Several executive orders have terminated government support for DEI programs. ■ Hospitals with DEI programs have been investigated for employment discrimination.
	Cap on federal loans for medical school	■ Recent legislation capped federal loans for medical students at $200,000 and eliminated living expense subsidies. ■ The reduction in assistance could discourage careers in underserved or nonprofit health care.
	Gender-related care restrictions	■ Several federal, state and judicial actions are in place or proposed to limit gender-related care, forcing many providers to limit services.
	Immigration actions and enforcement	■ Executive orders, which may force many to new visa restrictions, suspensions and delays for work visas could affect foreign graduate medical students. ■ Enforcement officers at hospitals and health care facilities could lead to fear and anxiety for some patients, families and employees. ■ Combined, the new policies could exacerbate existing labor shortages.[11]

[5] "No Place to Hide: Children Will Be Hurt by Medicaid Cuts," *Manatt Health and Lucile Packard Foundation for Children's Health report*.
[6] "Allocating CBO's Estimates of Federal Medicaid Spending Reductions Across the States: Enacted Reconciliation Package," *KFF website*.
[7] "Impact of Trump tariffs on US medical device market," *Medical Device Network website*.
[8] "For hospitals, tariffs could mean higher prices 'almost immediately,'" *Chief Healthcare Executive website*.
[9] "FY 2026 NIH Budget Request Overview," *American Educational Research Association e-newsletter*.
[10] "Children's Hospitals Graduate Medical Education (CHGME) Payment Program," ***HRSA Health Workforce website***, https://bhw.hrsa.gov/funding/apply-grant/childrens-hospitals-graduate-medical-education
[11] "Attacks on Immigrant Workers Undermine the U.S. Care Economy," ***The Century Foundation website***.

Disruption likely to accelerate market impacts

As the headwinds converge on pediatric providers, the market is likely to see a mix of responses, including:

- Reduction in pediatric capacity – fewer inpatient beds, fewer pediatric-focused clinics and providers
- Mergers of providers to create scale and balance payer mix
- Partnerships that can infuse capital and bolster financials
- Doubling down on the few services that are margin positive, such as neonatal care, surgical care and cancer care

Success will be achieved by the providers that make tough decisions on spending cuts and efficiency; compete aggresively on growth, payer mix and margin-positive services; and do not lose sight of their mission.

While it might be tempting to act quickly, providers that use this moment as both a catalyst for change and an opportunity to position for growth will find themselves as market leaders.

Every strategy will be unique given an organization's mission, history, population and competitive landscape. There are four domains that will help executive teams be comprehensive in their scenario planning and design:

Recommended actions for pediatric providers

1 Redefine vision and strategy

In times of disruption, a clear, focused strategy is essential.

It is tempting for pedratic care to move directly to actions such as cutting costs, programs and people as a reaction to the headwinds they are facing. While cuts are inevitably necessary, how, why and when can mean the difference between positioning for future growth and a downward spiral of cost cutting. Strategic actions executives can take include:

1. Examining strategic goals, approach and timeline

2. Considering viability, partnerships and M&A

1. Examine strategic goals, approach and timeline

Whether the organization just finished a strategic plan or it has been a few years, now is the time to re-evaluate. Market disruption in any industry should cause organizations to pause, examine potential risks and opportunities, and re-evaluate their strategic plans.

Ask questions such as:

- Do our strategic goals still make sense?
- What opportunities might be available that weren't a year ago?
- Are we ready to make tough decisions that we weren't ready for before?
- Are the timeline, staging and prioritization still right?
- Are we balancing the headwinds today with our future sustainability?
- Will we be in the financial position to execute? If not, can we be?
- How do we build more agility and flexibility?

Take the time to reprioritize, establish new targets and timelines, and design a strategic plan that can be managed in a dynamic environment.

2. Consider viability, partnerships and M&A

Whether the outcome is a new direction or confirmation of the current structure, pediatric providers should evaluate the benefits and drawbacks of joint ventures, affiliations, M&A, and private equity (PE) or PE-like partnerships. Conversations about a wider array of strategic options — which may not have been on the table previously — are likely to become more commonplace as the long-term viability of pediatric financial models is questioned.

Benefits of a partnership can be tempting, including access to capital, increased scale, shared risk and new capabilities. But drawbacks should also be carefully weighed, including loss of control, reduced ability to focus on the mission and mismatched priorities.

Over the next few years, the market will continue to see mergers, acquisitions, joint ventures and other innovative partnerships within the pediatric provider space to combat increasingly difficult market and regulatory conditions. A comprehensive assessment of options, due diligence and transaction guidance can support health systems in finding and executing the partnership that is right for them.

2 Explore revenue opportunities

A laser focus on revenue optimization opens doors for investment

Even before the current changes, existing market headwinds were pushing many pediatric providers to consider their revenue options. At this moment of disruption, a clarity of focus on revenue is essential; to achieve this, health leaders can:

1. Examine underperforming businesses
2. Balance the insurance mix
3. Focus on philanthropy
4. Consider value-based care and risk models (if appropriate)
5. Explore revenue diversification (if appropriate)

1. Examine underperforming businesses

Over the last decade, many health systems have expanded to adjacent businesses to diversify, including purchasing or building assets such as home health, urgent care and commercial insurance, either alone or through partnerships. Some ventures have been successful, while many others have struggled to achieve profitability and meet the pro forma expectations.

The current environment provides a healthy prompt to re-evaluate those businesses and determine whether each is still a strategically important asset or an investment that did not materialize, making it time to exit the business.

2. Balance the insurance mix

A harsh reality in the US health care system is that financial viability is reliant on an insurance mix that includes a significant portion of commercially insured patients.

With over half of all children in the US covered by Medicaid and the Children's Health Insurance Program (CHIP), and substantially higher in some geographies, it is especially important for pediatric providers to balance their insurance portfolios.

To attract commercial patients, providers should ask:

- Do I have the right services in the right locations?
- How is my patient and family experience (e.g., with facilities, digital assets, people, wait times, hours)?
- Am I providing the services and amenities expected?
- How is my brand and word of mouth?

3. Focus on philanthropy

Care for children has long relied on the generous support of donors to bridge the gap between services needed and reimbursement available, as well as to fund research, innovation and facilities. Given the significant changes outlined above, the requests for donors (individual and corporate) to fill the void of federal funding will be significant.

Verifying that the organization has a comprehensive, thoughtful and targeted philanthropic strategy for the current environment is essential.

4. Consider value-based care and risk models

For decades, value-based care has held the allure of better care for patients and healthier margins for providers. The reality has been mixed, with many providers discovering that the infrastructure and culture shift to achieve those results is significant, and trying to live in two systems — fee for service and fee for value — is exceedingly difficult.

Providers have also found commercial payers less interested in partnering than they might initially expect. For providers well positioned to succeed with a willing payer partner, risk models provide an avenue for vertical integration and new margin that should be explored.

5. Explore revenue diversification

Revenue diversification has been a successful strategy for some systems to spread risk and improve margin. These efforts commonly include drug development, commercialization of data and assets, selling back-office support as a service, and venture capital or incubation efforts.

Success is often linked to brand, research breakthroughs, investment capital and, sometimes, a bit of luck. If revenue diversification is a goal, confirm that efforts are directly supportive of the organization's strategy and its unique competitive advantage — along with appropriate investment, a built-for-purpose operating model and leadership expertise.

3 Drive efficiencies

Margins are compressing. Future success is directly tied to an organization's ability to provide high-quality care at a lower cost.

Our health care delivery system is notoriously complex and inefficient. Attempts for meaningful efficiency improvements are often halted by cultural barriers, previously failed attempts, incremental improvement and lack of sustained focus.

To use this moment of disruption as a catalyst for change, executive teams must execute differently than in the past. In designing a path to financial sustainability, leaders should explore three areas:

1. We should have done it before
2. It's always worth looking at revenue cycle
3. We need our most expensive assets to work efficiently

1. We should have done it before

These are the efficiencies that are no surprise to anyone. For a variety of reasons, the underlying causes of inefficiency haven't been addressed, and the current environment is a catalyst to take action. Whether the lingering inefficiency is a clinic that is consistently running at 20% productivity or physicians who are allocated 80% clinical time but only working 40% clinical time, these are issues that are no secret and need to be resolved.

Common exploration areas include:

- Productivity expectations and reporting
- Compensation structures and incentives
- Dashboards to easily monitor efficiency metrics

2. It's always worth looking at revenue cycle

With anticipated revenues decreasing from Medicaid cuts, shifts to outpatient settings and potential 340B reductions, pediatric providers need to confirm that they are collecting the revenue they have earned.

If you have not had an external assessment of your revenue cycle processes in a few years, it is worth a refresh. Look for deterioration of leading practices in coding, authorization, denial management, new barriers to collection that have emerged and new solutions — including AI tools — to improve collections.

3. We need our most expensive assets to work efficiently at operating rooms (ORs), NICU beds, infusion suites, MRIs and inpatient beds

Much of the revenue and margin of pediatric providers comes from a few assets and service lines. Taking the time to focus on their success is essential, including understanding opportunities, defining the cost and disruption required, and quantifying success.

Success in these areas is often tied to getting the basics right. Using ORs as an example, whether that is designing a productive block schedule, facilitating on-time starts or reducing turnover time in ORs, the basics go a long way toward opening capacity. If investment dollars are available, new software and analytics can optimize throughput and staffing to generate more productivity through the same footprint.

The effort to achieve these results should not be minimized. It takes sustained focus, collaboration and analysis to understand the opportunities and achieve results.

4 Expand cost-reduction efforts

The agility necessary to succeed in the coming years will come from a lower, focused cost structure.

Most systems are in a near-constant cycle of evaluating costs, and, in many cases, the "low-hanging fruit" has been cut. That leaves more difficult cost-reduction decisions to evaluate. Questions should include:

1. Where are we willing to act that we were not before?
2. What is essential to future growth and competitiveness (and what is not)?
3. Where do we accept "failure" and move on?
4. What fits into our new operating model (and what does not)?

This is the time to ascertain whether executives and board members understand the current cash position, areas of risk and cash management options as they explore decisions in the following areas with a new lens:

- Traditional levers — supply chain, labor, outsourcing
- Technology — automation, AI, self-service, robotics
- Portfolio rationalization — programs, geographies, locations

Traditional levers

Supply costs: Usually managed through a group purchasing organization, providers should proactively work with their vendors to manage potential impacts of tariffs and explore additional avenues for reducing spending growth on supplies.

If the organization has not completed a medical device rationalization, that should be completed early to harmonize devices and appropriately reduce spending.

Organizational spans and layers: An organizational assessment will evaluate when the organization appears "heavy" in the number of management layers, which can add costs and increase bureaucracy. It will also assess the span of control of managers to understand if any reductions could be achieved while maintaining performance.

Real estate: Many systems are still adjusting to the post-pandemic work environment, which can involve a hybrid work environment, collaborative space instead of individual offices and a reduced need for square footage for back-office services.

For patient-facing real estate, an assessment of consolidation potential and revenue per square foot can be used selectively reduce the footprint. Instead of having three clinics, a stand-to imaging center and lab space within a square mile, consolidating into one multispecialty space could add benefits for patients and finances.

Outsourcing/onshoring: As margins are continually compressed, a new look at what functions need to be controlled within the organization and/or which functions need to be co-located with other operations provides an opportunity for cost reduction.

Technology

Technology can be a powerful efficiency lever that requires up-front investment and implementation disruption to achieve gains. Depending on the profile of the organization, technology can position the organization for future cost reduction.

Automation: Usually confined to back-office functions, evaluating opportunities for automation to reduce overall headcount while creating a higher-paid supervisor position can simultaneously improve output, reduce costs and create upward mobility options.

Self-service: Creating opportunities for patients and families to order inpatient meals on a mobile device, check in for an appointment, pay bills online, and schedule and modify appointments online has the potential to improve patient experience, reduce headcount and improve service levels. The major caveat is that consumers expect a seamless experience, so investing in these applications with a frictionless experience is important.

AI-enabled applications: Though adoption should be cautious and thoughtful, AI has the potential to drive efficiencies throughout the back office and within clinical care, with the most common applications being ambient documentation, clinical decision support and virtual assistants.

Robotics: An option that is likely only for systems with a healthy investment tolerance and inclined to push innovation frontiers, leveraging robotics to reduce non-skilled and undesirable positions has the potential to both reduce costs and facilitate consistent operations in the long term. Whether delivering meals, transporting patients or lifting patients within the room, robots can complete the tasks humans would prefer to avoid.

Portfolio rationalization

While it is a difficult exercise, an assessment of programs, services and locations is likely required. It is common to have programs that were once funded by a grant or philanthropic support that has since run out or a personal project that was easily funded when margins were higher, or an expansion location that just did not materialize as expected.

The outcome of the assessment is to categorize programs, services and locations into the following categories: grow, keep, partner, sell, shutter.

Evaluation criteria should balance mission and financial sustainability:

- How is the program funded (e.g., grants, philanthropy, operating margin, mix)?
- What is the cost of the program to the organization?
- What does success look like, and how is it measured?
- How successful has the program been to date?
- How does the investment and impact of this program compare with others?
- Does the program create revenue for the organization?

SUMMARY

Pediatric providers' ability to pivot while staying dedicated to their mission is crucial.

Disruption will accelerate existing trends of consolidation and shrinking capacity. Organizations that emerge as leaders will have designed and executed proactive strategies that navigate the current climate while focusing on future competitiveness and growth potential. They will weather tough decisions and difficult trade-offs with a clear vision for the future that brings the organization with them.

Pediatric providers care for the most vulnerable in our society. Their ability to adjust course with an unwavering focus on their mission is vital to ensuring that the care we all want for our nation's children is available.

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