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The Changing Business Model For Colleges And Universities

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I write about strategic financial issues in higher education.

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Colleges and universities face daunting challenges to long-established business models. The cost of providing higher education continues to rise with fewer students either able or willing to pay the price. Competition among institutions for students has increased especially between public and private institutions; this is exacerbated by the demographic changes in the country whereby the number of high school graduates has decreased in most of the country and will not increase again until 2024. Compounding this problem is that the decrease in graduates from religious and private high schools is projected to be much greater than from public high schools. In addition, competition for students will further increase at private colleges and universities with the adoption of "free college programs" in various states and localities which are spreading like wildfires; there are now more than 200 such programs around the country with New York being among the most recent and the largest.

Resources are continually more difficult to generate. The average annual return on endowments over the last ten-years is 5% which is only slightly above the average spending rate of 4.4%. This does not allow endowments to keep up with inflation and is likely to lead colleges to reevaluate their spending policies which provide for spending rates between 4% and 5%. Tuition at private institutions has increased by 54% over the last ten years while net tuition per student has been almost flat as the tuition discount rate has approached 50% for new students. At public colleges, tuition has increased 62% over this same period due in large part to anemic funding from state and local governments in support of higher education. Further worsening this challenging climate, the public is beginning to question the value of higher education given the large debt incurred by students and their often perceived poor prospects for employment. Although this is the public perception, data shows that the return to a college degree ranges from $600,000 to $1.3 million compared to a high school degree and the average unemployment rate for college graduates did not reach 5% during the 2008 recession.

To ensure financial sustainability, many colleges and universities are responding by experimenting with changes to their business models. Historically, many of us advised institutions to "stay in their lane" meaning that they should stick with their mission no matter how narrowly defined. The advice was just to execute better on what you were good at doing. Today, I think most colleges with narrowly defined mission statements especially those which are primarily undergraduate liberal arts institutions need to think very seriously about moving outside their lanes. There are some schools which have made very large changes to their business models and have recreated themselves as very different institutions from the way they began.

Most prominent among these schools is Southern New Hampshire University which until 1995 was a relatively traditional college on 300 acres in Manchester, NH offering bachelors and master's degrees. In 1995, it launched an on-line program. By 2002, the on-line program had significant enrollment and today it has over 80,000 students while the traditional campus-based program continues with more than 5,000 students. In 2009, it added the SNHU Advantage Program which allows people to work full-time and receive an AA degree at a 60% savings from SNHU's regular undergraduate tuition rate. It has recently added College for America, a competency-based and project-based program which is to be "radically affordable" and workplace relevant delivered through employer partnerships. Other institutional innovators include Georgia Tech which began offering a Master's in Computer Science in collaboration with Udacity and AT&T on-line in 2014 and has just added an on-line Master's in Analytics both for $10,000 for the whole program although many students are able to complete the MS in Computer Science program for less than $7,000. Arizona State has partnered with Starbucks to offer the Starbucks Achievement Academy and has just begun the Global Freshmen Academy which offers courses to freshmen all over the world on-line for $200 a course and the student only pays after completing the course. Another model is exemplified by the proposed Purdue-Kaplan relationship which will bring together a traditional public research university with a for-profit on-line institution if approved by the Higher Learning Commission this month. And there is Sweet Briar College, a woman's college in Amherst, VA which is reinventing itself after almost closing in 2015. With a new president since May, 2017, the College has changed its term structure, redone its core curriculum, created three interdisciplinary centers of excellence in place of traditional departments and reduced its tuition by $15,000.

More prevalent and smaller scale changes to the business model relative to activities to increase enrollment and net tuition revenue include changes to pricing and discounting policies; additions of new programs to increase institutional attractiveness, especially pre-professional programs; recruitment of new student populations including part-time, transfers and international students. More and more institutions are considering resetting their prices down as the gap between the published price and the average price paid reaches 50% at private institutions. Many institutions are partnering with third party providers to put programs on-line usually using revenue share agreements that minimize risk to the institution. These changes often take an institution beyond its originally stated mission. The majority of the institutions which have been successful in increasing their revenue stream from students have broadened their missions and many have strayed far outside their initial lanes.

In terms of changes to the business model on the cost side a variety of strategies to reduce the cost of running colleges and universities are being implemented. These include the continued reduction in the percent of full-time faculty at private institutions which has declined from 78% of the faculty in 1970 to 51% today and the decline in tenured faculty among institutions with tenure which, in the last 20 years, has fallen from 50% to 44%. Beyond changing the composition of faculty, schools are offering programs in different formats including on-line and hybridwhich increase accessibility of the programs and minimize facility use. Forward-thinking institutions are working to minimize their idle capital by using their campuses much more fully year-round. A few campuses now operate year round with three terms where groups of students are required to attend the summer term.

As schools become more resource constrained, there is increased consortia activity to minimize costs in many areas ranging from health care, insurance and retirement administration and endowment management to academic programs with limited enrollment being jointly offered by two or more institutions. Schools are partnering with businesses to leverage private capital to make infrastructure and other facility additions and improvements using revenue share and savings share agreements. In terms of reducing costs to students, many schools are using open courseware instead of expensive text books and reducing time to degree. As I look to the future, the successful colleges will need to look for ways to become more efficient in their delivery of education if they are to be able to maintain their quality.

Among the cost saving initiatives with the greatest potential will be collaborative activities among institutions and with new partners, public and private even including mergers in some cases as well as the de-siloing of institutions. Successfully implementing such strategies will require trust among all participants and the recognition that going it alone may no longer lead to the best outcomes. But the bottom line is that the higher education industry will remain under stress until it can develop a new financial model to provide a quality education at an affordable price to students.

Most other industries facing similar conditions would contract. Yet, colleges and universities rarely shut down given the power of tradition and faithful alums. But are our students and nation best served by continuing to maintain a plethora of institutions, struggling to attract adequate numbers of students and continually reducing costs to keep their doors open? Would the industry be better off with fewer, better financed institutions?

Note: Slight corrections were made to information on Sweet Briar and Georgia Tech. The author is consulting at Sweet Briar.

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