For College Finances, There’s No ‘Return to Normal’

The critical problems facing higher education won’t end with the pandemic.

THE REVIEW

By Mark S. LeClair
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Higher ed is in trouble. It faces a demographic crunch in 2026, when smaller high-school graduating classes will mean greater competition for students. That will lead to tuition discounting and underenrolled classes for many colleges. And yet that demographic crisis is only one of many significant challenges the sector faces. As noted by Forbes in its annual review of college and university financials, approximately 20 percent of all institutions now warrant a “D” ranking (its lowest). Many are under serious financial strain and may not survive.

Which of these colleges are truly at risk? The past provides some clues. Since 2016, colleges have failed for many reasons: changing demographics, fewer students with a religious background (impacting the many small colleges with a religious affiliation), a drop in interest in single-sex institutions, and changing student preferences for urban over rural environments. Long-established, heavily endowed elite institutions will be fine, of course, but smaller colleges vulnerable to these changes will struggle. While they may not fail, they will need to brace themselves for uniquely difficult financial circumstances.

Among the dozens of casualties over the past five years were several institutions that had been in operation for over 100 years, including St. Gregory’s University, in Oklahoma; Marylhurst University, in Oregon; Green Mountain College, in Vermont; and the College of New Rochelle, in New York. Covid-19 has only made things worse. Several colleges that were in a weakened state already have been pushed out of existence over the past year, and others have declared financial exigency, including public institutions such as Central Washington University and Missouri Western State University. As the pandemic’s negative effects continue, it seems likely that additional institutions will be forced to take the same path.

The pandemic has also produced disruptions never seen before in higher education. The mass migration to online learning — which emptied out dorms and cafeterias and forced colleges to refund millions of dollars in fees — was financially painful. Most institutions could absorb a one-time blow of this magnitude, which we saw in the spring of 2020. But as online and hybrid
instruction became the norm into the fall, room-and-board revenue continued to suffer. Money borrowed to build housing cannot be paid back with the revenue from half-empty dorms.

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Most colleges are planning for a return to in-person, residential learning this fall, but the accepted mode of instruction may have been permanently swept away by the pandemic. Returning fully to “normal” is likely impossible as hybrid (both synchronous and asynchronous) instruction has become widely ingrained. Covid-19 also destroyed revenue streams that had taken years for institutions to develop, such as income from foreign students. Arrangements like these are likely to be suspended for multiple years, and it will take considerable time to rebuild them.

Although the sudden forced refund of student room-and-board charges was a damaging impact of Covid-19, the reality is that it exposed a problem that has been building for some time, and one that colleges have done little to prepare for: As online and hybrid education advances, the need for on-campus housing and dining services will decline. Colleges, in their role as landlords, will experience a decline in this stream of revenue, and there is little that can be done to reverse it. Some colleges may be able to rent housing to faculty and staff as an interim measure to offset a declining student presence on campus, but local zoning authorities are unlikely to permit institutions to rent student housing to the general public, and such a move would likely threaten their nonprofit status.

A more fundamental challenge facing colleges is the changed perspective of what higher education is supposed to offer. Those who attended college in the 1970s and 1980s, even at top-tier institutions, lived and studied in facilities that would be regarded as wholly unacceptable today. Old and cramped dorm rooms, mediocre food, and aging labs and libraries were the norm. College was mostly a place to learn, and the amenities that are commonplace on campuses today were nowhere to be seen.

Colleges have, over the past 50 years, engaged in an unwinnable battle to outdo competitors with ever-increasing amenities. Visiting students and their parents expect a brand-new library, top-notch athletic facilities (even for non-athletes), superior dining, and frivolities unrelated to the core mission of the college (rock-climbing walls, floating rivers, and hot tubs). Institutions that do not match the amenities of their competitors fall behind and see applications dwindle.

Institutions have been forced into a game of one-upmanship — and there are no winners. Having more gleaming, new facilities does not mean more students when you consider the entire sector is engaged in providing such amenities. If the market for a college education were more concentrated — if there were fewer institutions — the futility of this exercise would become
obvious, and the competition to offer ever more and better facilities would cease. And yet we play on.

This competition is also playing out on the programmatic side. As undergraduate enrollments fail to rise, even with ever-deeper discounting, colleges are turning to newly created graduate programs as incremental revenue streams. This is a reasonable response, but as more and more institutions start similar programs, the outcome is going to be the same: a marginal increase in enrollments, coupled with rising costs.

Those costs will be harder to pass on to students, who are becoming more aware of their ever-increasing amounts of debt, the total of which rose from $480 billion in 2006 to $1.6 trillion in 2020. Although this is a staggering sum, the earnings premium that a college degree provides is still large. The problem for colleges is the growing perception among students and their families that there is a debt-load crisis. This causes some students to decide against going to college and many others to choose a “practical” major that will help them in the job market. The latter represents an enormous challenge for colleges, as the tenure system prevents institutions from rapidly adjusting curricula to changing student interests.

None of the impacts arising from these challenges will be good for academe, nor for the faculty and administrators who have made higher education their livelihood. Retrenchment, whether under financial exigency or simply through sustained elimination and downsizing of programs, is inevitable. Also inevitable is the failure or merging of numerous smaller institutions that do not have the resources to weather the current financial pressures or the coming demographic cliff.

Although it is considered anathema to discuss retrenchment, a medium-term strategy of reducing size of operations may be one of the most promising ways to approach the next five years. Many colleges would be better off delaying the building of new dorms (or accelerating the retirement of older ones). Fewer debt and maintenance obligations would enable a college to withstand small, stepped drops in enrollment until the demographics reverse. Marginally lower enrollments would enable delays in the hiring of faculty, administrators, and staff.

Strategic plans are critical, especially with the inevitable rise in online and hybrid education. The wholesale switch to online learning during the pandemic has resulted in a change in attitudes on the part of faculty and students toward what learning should look like, and that change is not wholly reversible. While a majority of students indicate that low-cost distance learning is inferior to in-class instruction, a sizable minority prefer its convenience. Institutions must carefully address the issue of dual modes of delivery and differential pricing. As some colleges discovered, students who paid the market rate for in-person instruction were less than pleased with the transition to online learning in 2020.
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Additionally, colleges should roll out new programs with the understanding that successful, innovative courses may be easily copied by rival institutions, and thus any benefits may be temporary. Colleges routinely conduct a market study before devoting resources to the development of a new program, but rarely does that entail an institutional-capacity analysis of competitors. If faculty participation is the only thing required for a new program, there is little stopping other colleges from getting in the game, while a new engineering or nursing program (requiring lab space and specialized faculty) is in far less danger of being duplicated in the near term. Incremental revenue streams should be viewed as a positive only if they are competitively sustainable.

Of all the problems facing institutions, resolving the dual-revenue-stream issue may be the most challenging. Dorms emptied out in March 2020 and, for the more fortunate institutions, partially refilled in September. Capacity limits remained in place in many states, so dorms were only partially filled in the spring of 2021. Many students have reported deep dissatisfaction with highly controlled dorm life, particularly rolling quarantines, and a sizable number may opt out of on-campus life in the near term, leading to a further deterioration in this revenue stream. Although institutions have enjoyed the profitability of being landlords and food-service providers, the near- and medium-term shrinking of capacity is essential if colleges want to avoid having auxiliary activities become a drain on net revenues.

The most dangerous strategy is no strategy. The *Forbes* financial analyses have been warning of a worsening situation for years. The added stresses from the Covid-19 pandemic will further aggravate the untenable circumstances facing hundreds of institutions. There is now a very short window within which we must carry out significant reforms. This will be a difficult five years for higher ed, but the painful transformations to come may have one benefit: Colleges will be forced to focus more on their central missions, and forgo some of the peripherals that have led our sector astray.

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*We welcome your thoughts and questions about this article. Please email the editors or submit a letter for publication.*

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