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# College Closures: Facts vs. Perception

July 28, 2022

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# AGENDA

- **Prognosticators:** Who Said What
- **Marketplace Realities:** Are the Prognosticators Right? Or Even Close?
- **Current Issues:** Factors Impacting Financial Health/Risk Factors
- **Making the Pivot**: Tactics for Pivoting from the Edge of the Cliff
- **Having the Right Tools:** Margin, Modeling, Management, & Leadership

# The Prognosticators

1. Clayton Christensen (Author, Harvard Business School Professor)
2. Tomas Frey (Former IBM Engineer, DaVinci Institute Founder, Futurist, Blogger, & Celebrity Speaker)
3. Moody's Investors Service (Bond Rating Agency for Mostly Stronger, Larger Institutions)
4. Robert Zemsky (Professor, Graduate School of Education—University of Pennsylvania, Author of the College Stress Test)

Others:

- Forbes (Financial Grades): For 2021, 65% at C or below, only 35% above a C (n=1,369 schools)

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# Clayton Christensen

2013 – “The bottom 25% of every tier of colleges will disappear or merge in the next 10 to 15 years”
Note: 10 years will be next year

2017 – Innovation & Disruption Conference – “Half of all American universities will close or go bankrupt within 10 to 15 years”

Later in 2017 – Salesforce.org Higher Education Summit – “I bet it takes nine years rather than 10” (Referring to an audience question about his belief that 50% of colleges close within 10 to 15 years)

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# Tom Frey

2010 – “By 2030 over 50% of colleges will collapse”

“The future of education will **revolve around hyper-individualized learning, self-paced, organically generated content that is modality diverse, & available on-demand 24/7. Any topic, anywhere, anytime** . . . it will be less dependent on teachers, less dependent on schools, & offer more personal control”




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# Moody's Investors Service

2015 – Closure rates for small colleges & universities will triple in the coming years, & mergers will double. Could lead to as many as **15 closures per year by 2017**

In the 25 years from 1990 to 2015, the average was five per year. Triple the 2015 rate would be 15. Did they come close?

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# Robert Zemsky

- In 2020, Zemsky writes
  - ✓ “10% of the nation’s colleges & universities face substantial market risk”. FORVIS Comment: *There are 1,687 private nonprofit colleges reported by IPEDS. That could mean nearly 168 schools are in trouble*
  - ✓ “30% bound to struggle”
  - ✓ “60% face little to no market risk”

Market risk means running out of students. Financial risk is running out of money. Zemsky equates the two. The College Stress Test, Robert Zemsky et al., Johns Hopkins University Press, 2020 Pg. 117

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# Marketplace Realities

Are the prognosticators right? Are they close?

- FORVIS Analysis of Closure Data
- Risk Factors for Closing

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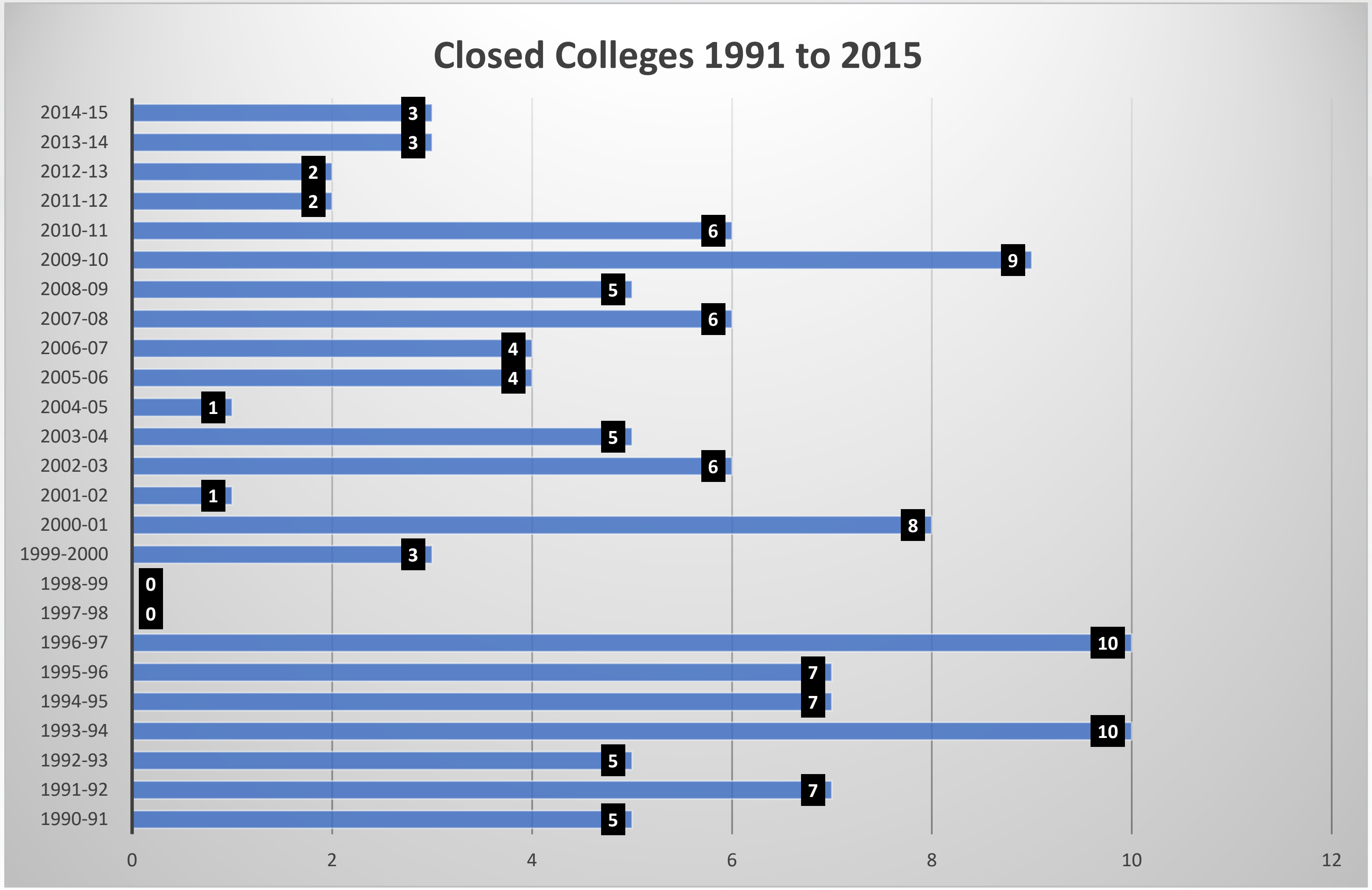
# FORVIS Closure Analysis

Early Years (1991 to 2015)

**Average closure rate: five schools per year**

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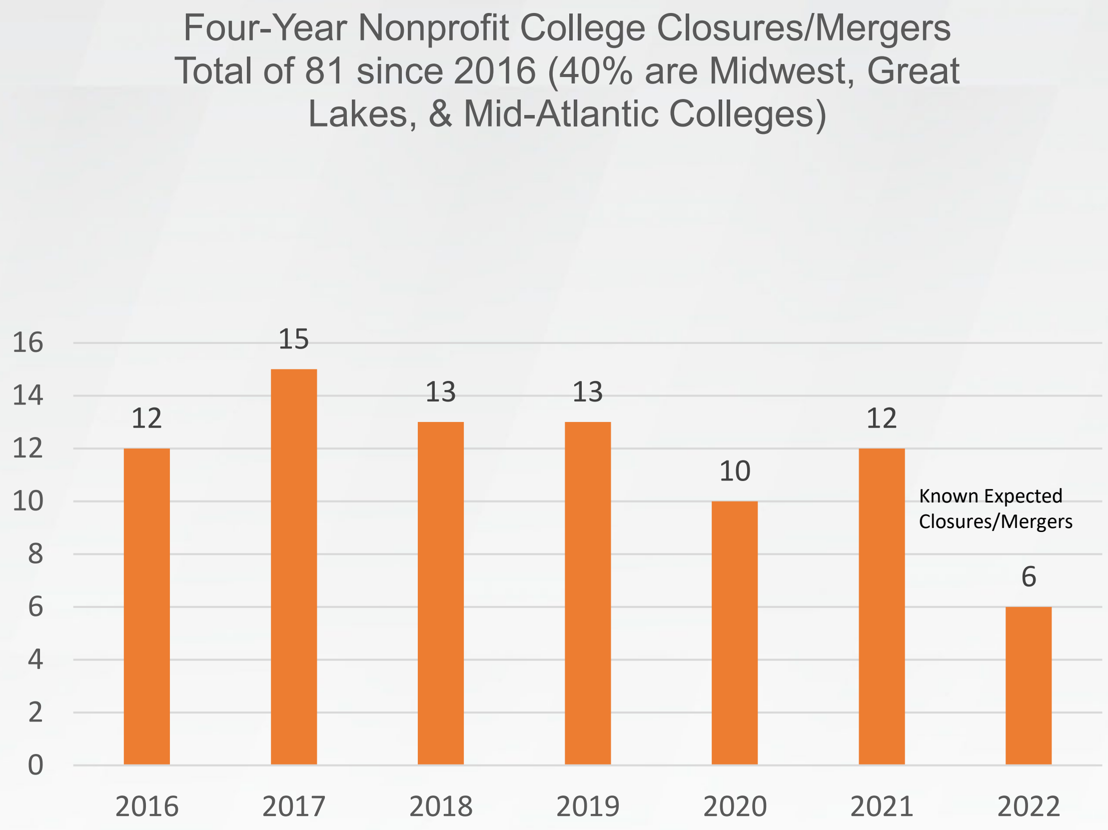
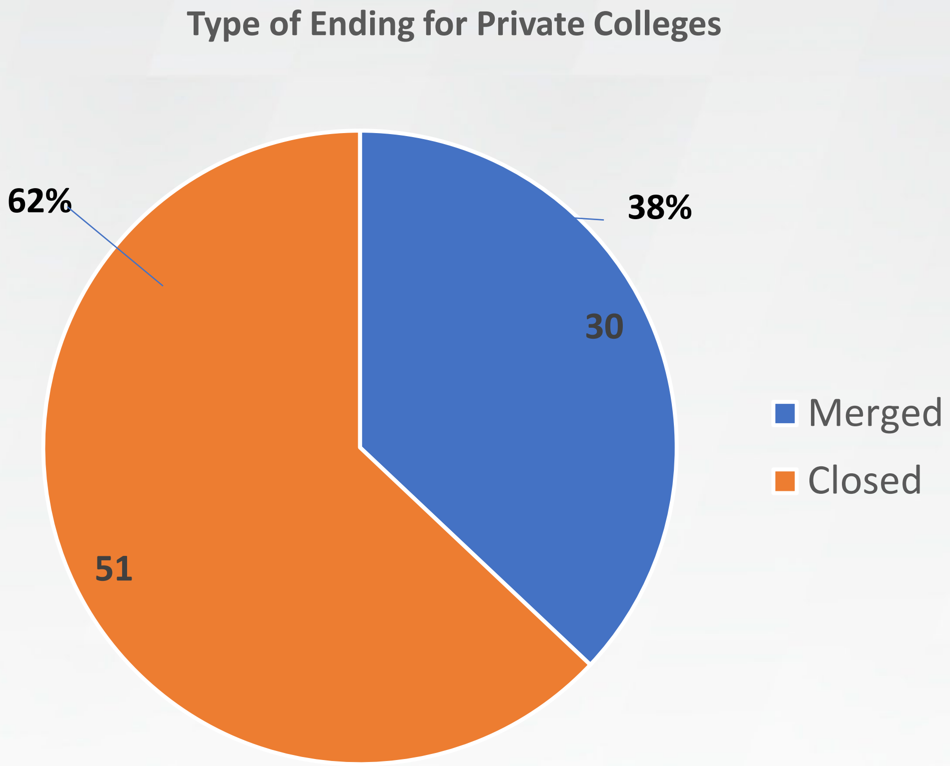
# FORVIS Closure Analysis

## Recent Years (2016 to 2021)

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# FORVIS Closure Analysis

## More Analysis

- Specialty Schools Included — 22 of 81 (27%)
  - Art Schools
  - Seminaries
  - Health Science
- Size at Closure — 708 (Average)
  - High — 7,800 (Health Sciences Merger)
  - Low — 23 (Seminary)
  - Median — 400

# FORVIS Closure Analysis

- Faith Based versus Secular — 47% Faith Based
- Geographical Spread

| | | | |
|---|---|---|---|
| Great Lakes | 16 | Northeast | 25 |
| Mid-Atlantic | 7 | South | 10 |
| Midwest | 9 | West | 14 |

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# FORVIS Closure Analysis

Did anyone get it right or come close?

**Moody's Investors Service**

*2015 prediction* – Closures to triple by 2017. 2017 number was three times the 25-year average of five per year (15)

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# How Did Moody’s Predict Closure Rate so Close?

Susan Fitzgerald, Senior Vice President in Moody’s higher education practice, says the ratings agency “starts with a quantitative assessment of factors like operating revenue, liquidity, & investments”

“But there are multiple other credit considerations that are unique to each institution that provide that forward look, & **the forward look is really in large part driven by management & governance,” she says. “That’s a much more qualitative assessment than any number or group of numbers will give you”**

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# How Should We View the Predictions?

## Rick Staisloff on use of metrics to predict closure

“The **danger is in overpromising what these tools can provide** to us”

“To the extent that we’re trying to predict what’s going to happen for higher education institutions going out of business, **I think that is enormously overreaching** — actually, I’d take that a step further and say **it’s irresponsible**,” says Staisloff. **Predictions about a college’s long-term viability can not only be wrong but can affect that institution’s ability to attract & retain students & hasten its demise**. “It’s trying to apply metrics in ways that I just don’t think are possible.”

As reported by Scott Carlson for the Chronicle of Higher Education, January 31, 2020

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# Risk Factors

Since the Great Recession, a common refrain heard throughout higher education is that hundreds of colleges & universities are at risk of going out of business. **The reality, of course, is that few have closed — about five a year, on average — lulling many academic leaders into believing that they are somewhat immune from the disruptive forces of change sweeping the economy**.

EY Parthenon: Strength in Numbers, 2020

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# Risk Factors – EY Parthenon White Paper (2020)

1. Enrollment under 1,000 students*
2. No online program*
3. Annual tuition increases of more than 8%*
4. Tuition discount rate higher than 35%*
5. Dependent on tuition for more than 85% of revenue*
6. Endowment that covers less than 33% of expenses
7. Debt payments more than 10% of expenses*
8. Deficit spending

* Mentioned in “Turnaround (2009)” list of 20 Risk Factors

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# A Study of Recent Closures of “Larger” Private Colleges

- Marygrove – Michigan (925)
- Concordia – Portland (5,000)
- Concordia – Bronxville (1,857)
- Wesley – Delaware (600)
- Martin Methodist – Tennessee (890)
- Becker – Massachusetts (1,500)

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# Closed College Financial Metrics (Last Year of Operations)

| Metrics Yr Before Closure | Wesley | Martin Methodist | Becker | Marygrove | Concordia Portland | Concordia Bronxville | Comments |
|---|---|---|---|---|---|---|---|
| Liquidity Ratio (Using Primary Reserve) | -0.35 | 0.07 | -0.07 | -0.38 | -0.05 | 0.03 | Low or negative liquidity |
| Net income from operations (Last Yr of Operations) | $ (698,631) | $ 112,295 | $ (795,590) | $ 1,904,576 | $ (5,020,671) | $ (1,184,279) | Operational Losses |
| Cash Flow from Operations | $ (784,483) | $ (341,798) | $ 1,058,068 | $ 1,380,392 | $ 2,626,487 | $ (944,154) | Half with Cash losses from Operations |
| Debt Service Coverage | 2.65 | 4.78 | 2.16 | 8.88 | -0.03 | 1.11 | Mixed debt service coverage (Moody's 2.76) |
| Days Cash on Hand | 37 | 24 | 15 | 66 | 54 | 17 | Very Low Cash on hand |
| Growth in net tuition | -4.05% | -3.68% | -1.00% | -41.59% | 14.37% | 27.95% | Net Tuition revenue not growing |
| DOE Ratio | 1.20 | 1.70 | 1.70 | -0.10 | 1.10 | 1.40 | In or below "Zone" |
| Investment income | $ 168,361 | $ 362,204 | $ 335,733 | $ 40,072 | $ 314,130 | $ 1,068,499 | Low Investment Income |
| Contribution Income | $ 2,322,706 | $ 1,275,194 | $ 1,381,845 | $ 6,594,134 | $ 3,930,319 | $ 1,683,755 | |
| Income/Deficit from Auxiliary enterprises | $ (1,273,255) | $ 1,792,935 | $ 732,182 | $ (113,138) | $ (2,574,420) | $ (1,642,742) | Most with deficits in Auxiliary Enterprises |

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# Closed College Risk Factor Review

| | | Risk Factors Over last 4 yrs | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| School Name | State | Enroll under 1,000 | No Online Program | > 8% tuition Increase | Discount Over 35% | Tuition Dependency >85% | Endowment Coverage <33% | Debt Payments >10% | Deficit Spending |
| Wesley College | Delaware | Yes | Online | No | Yes | Yes | Yes | No | Yes |
| Martin Methodist | Tennessee | Yes | Online | No | Yes | Yes | Yes | No | Yes |
| Becker College | Massachusetts | No - 1,500 | Online | No | Yes | Yes | Yes | No | Yes |
| Marygrove College | Michigan | Yes | No | No | Yes | Yes | Yes | No | Yes |
| Concordia College, Bronxville | New York | No - 1,857 | Only 1 | No | Yes | Yes | Yes | No | Yes |
| Concordia College, Portland | Oregon | No - 5,000 | Online | No | Yes | Yes | Yes | No | Yes |

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# DOE SCORES GIVING FALSE HOPE

| | Coleman University, CA | Grace University, NE | Green Mountain College, VT | Marylhurst University, OR | Judson College, AL | Mount Ida College, MA | Newbury, MA | Saint Joseph College, IN | Southern Vermont College, VT |
|---|---|---|---|---|---|---|---|---|---|
| Year Closed | 2018 | 2017 | 2019 | 2018 | 2021 | 2018 | 2018 | 2017 | 2019 |
| Last DOE Score | 2.3 | 1.70 | 1.30 | 2.20 | 2.10 | 0.80 | -0.10 | 1.40 | 2.0 |
| DOE Score 2016 | 1.2 | 0.60 | 0.20 | 2.20 | 1.20 | 2.10 | 1.70 | 1.40 | 1.90 |
| DOE Score 2012 | 3.00 | 2.10 | 1.50 | 2.40 | 2.20 | 1.50 | 2.60 | 2.20 | 2.40 |

**DOE Financial Responsibility Score Interpretation**

| Not Financially Responsible | Flagged for Monitoring | Financially Responsible |
|---|---|---|

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# Factors Most Impacting Financial Health

1. Enrollment
2. Academic program margin
3. Administrative cost structure
4. Debt/Liquidity
5. Endowment focus & size

*Unable to generate adequate net income from operations*

*Inadequate endowment to cover for lack of academic program margin*

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# Revenue Cost & Margin Analysis

## Private School #1 – Medium Size School

### Enrollment 2,502 (’17) | Endowment $13,129,960 | Grad School: Yes

Academic Programs

| | | | |
|---|---|---|---|
| Instruction | | | |
| | Tuition & Fees | $ 41,655,470 | |
| | Less Institutional Aid | $ (15,495,387) | -37% |
| | | | |
| | | | |
| | Government Appropriations | | |
| | | | |
| | Instruction | $ (18,449,103) | -44% |
| | | | |
| | | | |
| | Margin | $ 7,710,980 | 19% |
| | | | |
| Margin Funding | | | |
| | Academic Support | $ (2,633,608) | |
| | Student Services | $ (9,809,024) | |
| | Institutional Support | $ (5,529,902) | |
| | Net Margin | $ (10,261,554) | -25% |

Auxiliary Enterprises

| | | | |
|---|---|---|---|
| Auxiliary Enterprises | | | |
| | Sales & Services | $ 6,293,136 | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | Auxiliary Service Expense | $ (6,993,619) | -111% |
| | | | |
| | | | |
| | | $ (700,483) | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | $ (700,483) | -11% |

Capital Management & Philanthropy

| | | |
|---|---|---|
| Capital Management & Philanthropy | | |
| | Investment Income | $ 1,180,482 |
| | Private Gifts – Nonoperational | |
| | Private Gifts – Operational | $ 2,833,180 |
| | Endowment Gifts | |
| | Interest Rate Gain on SWAP | |
| | Change in Value - Split Interest Gifts | |
| | | |
| | Interest on Operating Funds | |
| | Other Income | $ 622,619 |
| | | $ 4,636,281 |
| | | |
| | | |
| | Interest Cost | Allocated |
| | Fundraising Expense | $ (94,201) |
| | Loan Cancellation | Allocated |
| | | $ 4,542,080 |

**Net Loss – $6,419,957**

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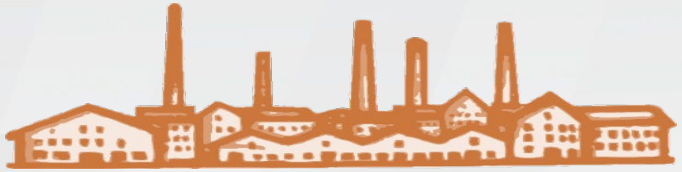
# Revenue Cost & Margin Analysis

## Private School #3

Enrollment 866 ('17) | Endowment $93,355,290 ($108K per student) | Grad School: Yes



### Academic Programs

| | | | |
|---|---|---|---|
| Instruction | | | |
| | Tuition & Fees | $ 31,379,970 | |
| | Less Institutional Aid | $ (19,500,988) | -62% |
| | Government Grants | $ 580,668 | |
| | | | |
| | | | |
| | | | |
| | Instruction | $ (13,369,231) | -43% |
| | | | |
| | | | |
| | Margin | $ (909,581) | -3% |
| | | | |
| Margin Funding | | | |
| | Academic Support | $ (2,819,984) | |
| | Student Services | $ (9,239,142) | |
| | Institutional Support | $ (8,638,370) | |
| | Net Margin | $ (21,607,077) | -69% |

### Auxiliary Enterprises

| | | | |
|---|---|---|---|
| Auxiliary Enterprises | | | |
| | Sales & Services | $ 10,408,296 | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | Auxiliary Service Expense | $ (5,980,279) | -57% |
| | | | |
| | | | |
| | | $ 4,428,017 | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | $ 4,428,017 | 43% |

### Capital Management & Philanthropy

| | |
|---|---|
| Investment Income | $10,982,811 |
| Private Gifts – Nonoperational | $ 8,380,320 |
| Private Gifts – Operational | $ 5,787,137 |
| Endowment Gifts | |
| Interest Rate Gain on SWAP | $ 1,636,243 |
| Change in Value – Split Interest Gifts | $ (26,771) |
| | |
| Interest on Operating Funds | |
| Other Income | $ 1,854,757 |
| Change in Beneficial Interest in Trusts | $ 618,164 |
| | $29,232,661 |
| | |
| Interest Cost | Allocated |
| Fundraising Expense | $(2,023,844) |
| | |
| | $27,208,817 |

**Net Gain – $12,053,601**

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# **Current Issues:** Factors Impacting Financial Health/Risk Factors

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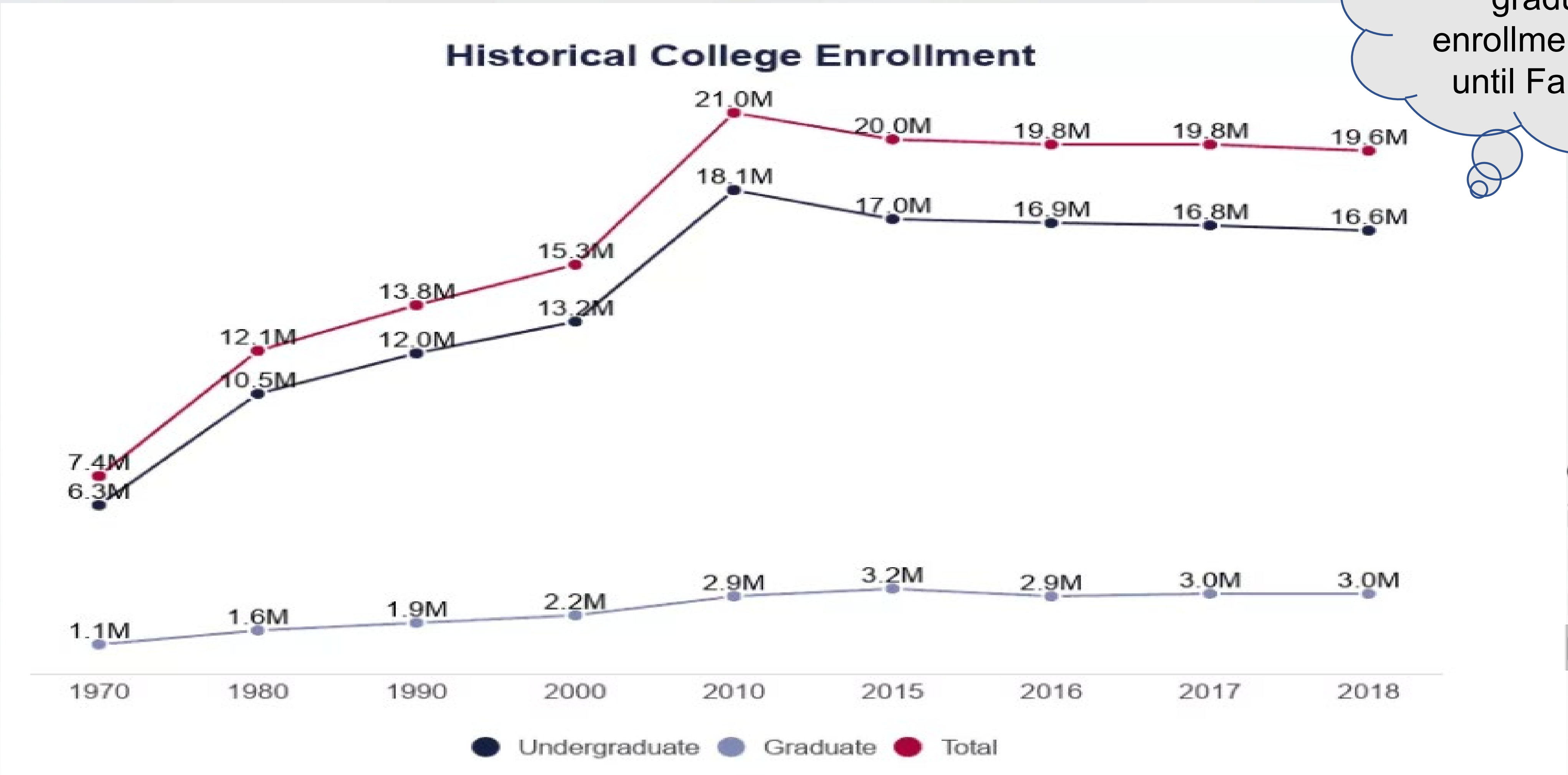
| By Institution type | Fall 2021 | Fall 2020 | Fall 2019 |
|---|---|---|---|
| Public 4-year | -3.0% | 0.2% | -1.2% |
| Private nonprofit 4-year | -1.6% | -0.1% | -0.6% |
| Private for-profit 4-year | -9.3% | 5.3% | -2.1% |
| Public 2-year | -3.4% | -10.1% | -1.4% |

## Change in total – All institutions


Chart: Natalie Schwartz/Higher Ed Dive • Source: National Student Clearinghouse Research Center • Get the data • Created with Datawrapper

# ENROLLMENT




Total enrollment falling, but graduate enrollment rising until Fall 2021

Graduate enrollment increases:

Fall 2019 0.80%

Fall 2020 3.60%

**Fall 2021 -0.40%**

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# Enrollment & the Coming Demographic Cliff

At a 2018 College Board Forum (Admissions and Financial Aid)…
Poll question used:

**What is your institutions response to the coming demographic changes to start in 2025 and after?**

A. Preparing for tighter budgets

B. Increase enrollment by widening access to more/different populations

C. Preparing to out-recruit the competition

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# Enrollment & the Coming Demographic Cliff

Answer to the 2018 Poll?

**C. Preparing to out-recruit the competition - 80%**

Note: It is mathematically impossible for all colleges to out-compete everyone else.

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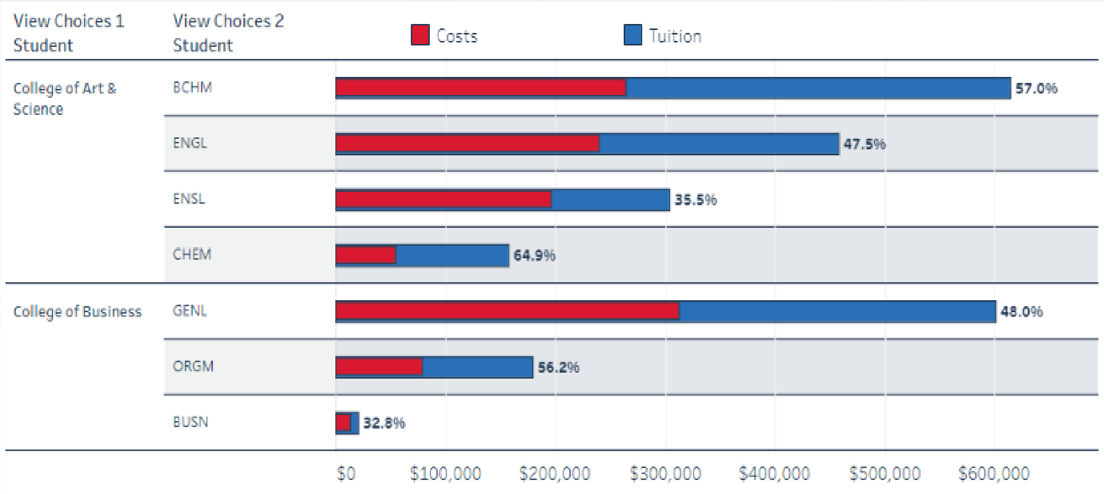
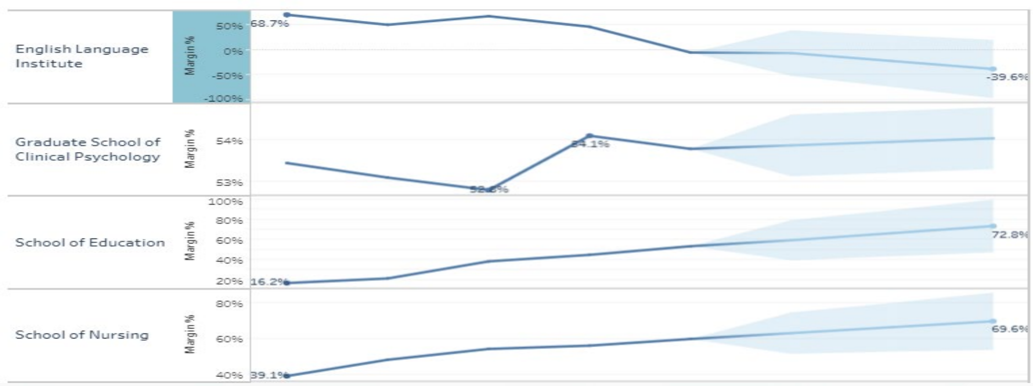
# Academic Program Margins

1. Are you measuring them?
2. Are you seeing the trends?
3. Are you using the data to make informed decisions?

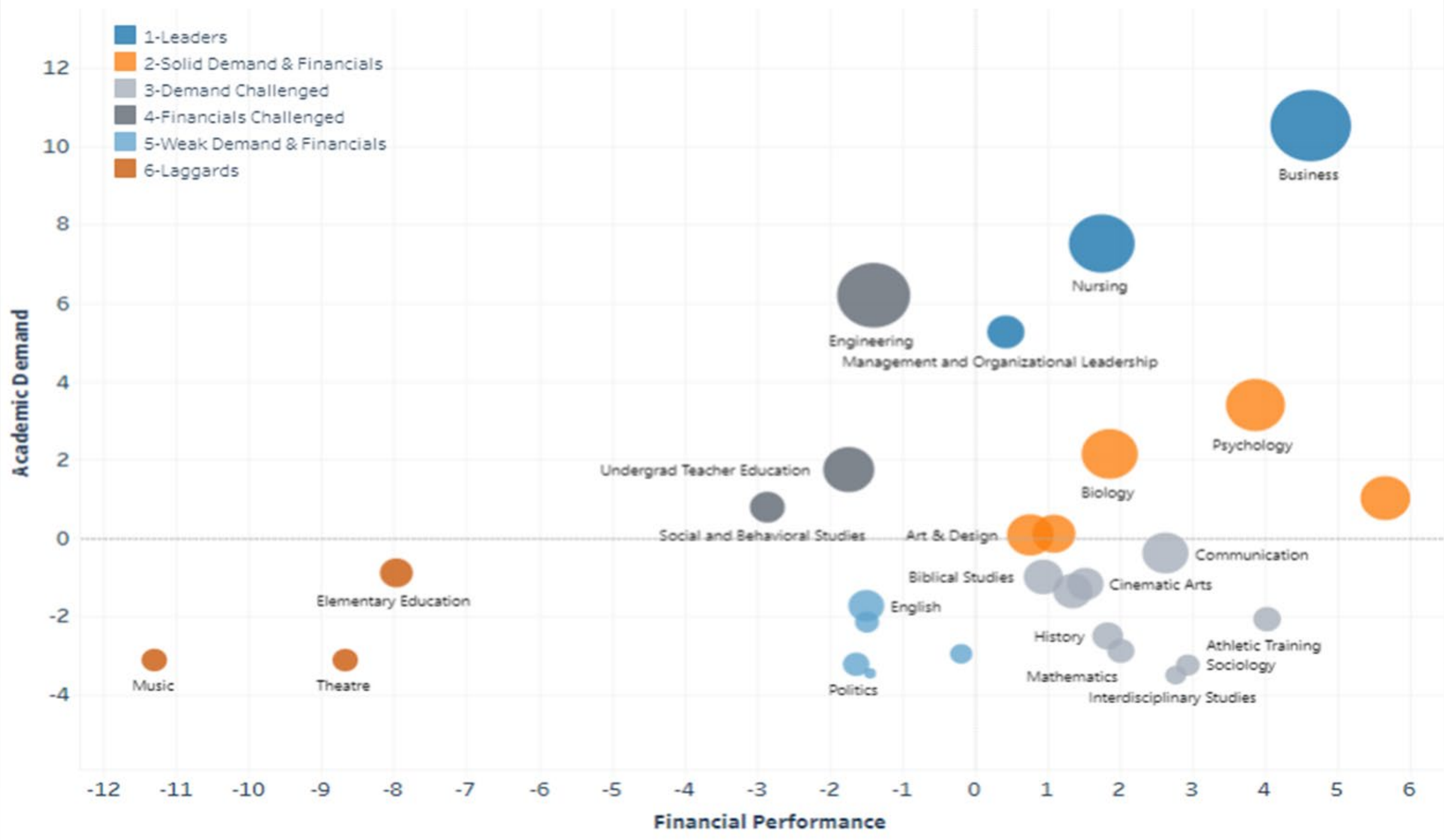


# Academic Program Analysis: Demand & Performance

## Integrated Approach:

## Academic and Financial Scoring

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# Enrollment

Tackling this issue successfully will take a multifaceted approach including

1. **New programs** (new subjects & new types of awards (Certificates, etc.))
2. **New populations** (ages, geographies, ethnic groups, etc.)
3. **New delivery systems** (online, hybrid, community based, etc., all while staying true to mission)
4. **Easier access** (better funding for student financial aid)
5. **Focus on quality** (improving retention & completion)

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# Administrative Cost Structure

Need to bend the cost curve down

1. Will help “sell” the Academic cost structure work that needs to be done. Builds a sense of shared sacrifice
2. Needs to be strategic. Don’t kill the goose laying the golden eggs (fundraising, marketing)
3. Needs an assessment of what really needs to be & by whom. Avoid duplication, focus on efficiency & effectiveness

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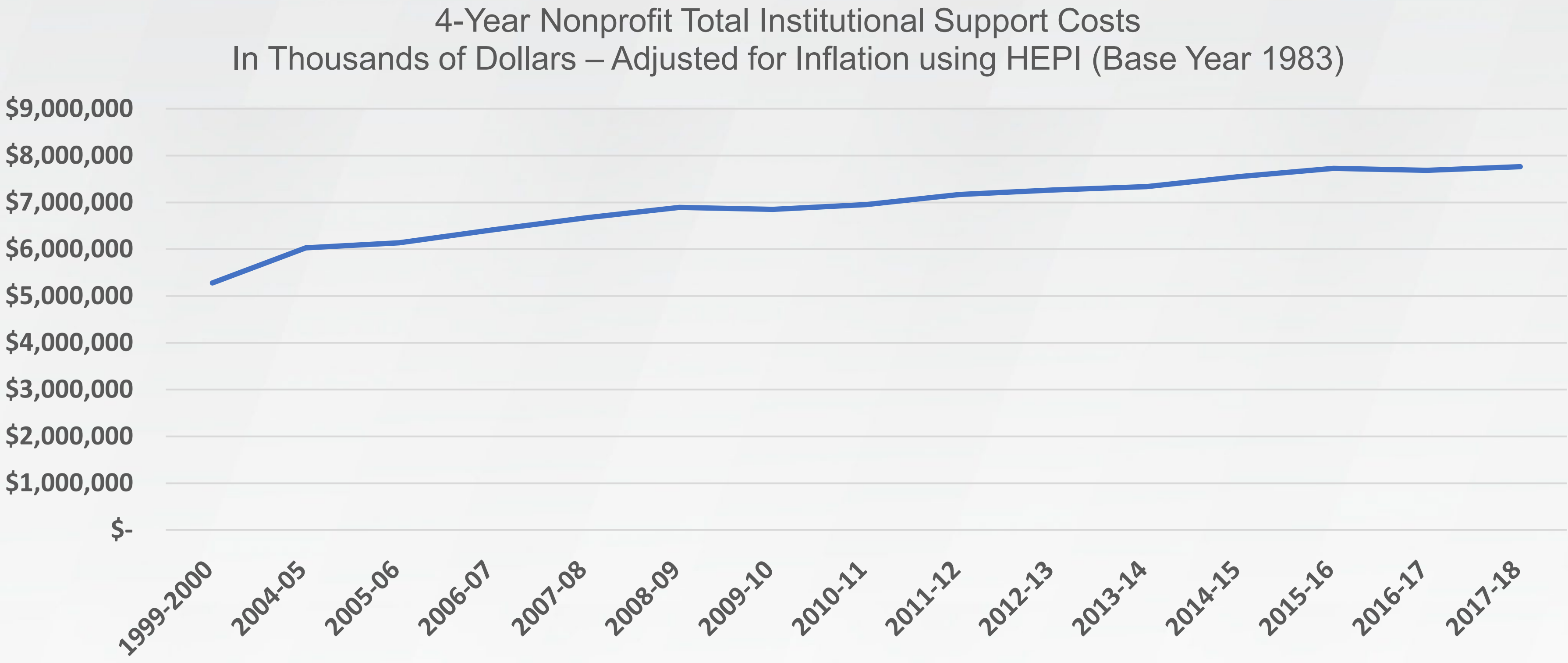
# Administrative Cost Structure – Private




https://nces.ed.gov/programs/digest/d19/tables/dt19_334.30.asp

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# Optimize Debt & Liquidity

Need a fresh look

1. Debt limits & term (finding opportunities for restructure)
2. Policies to guide borrowing (debt types & amounts)
3. Policies to guide building or maintaining liquidity (how much is enough; appropriate floors & ceilings; composition)

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# Liquidity & Debt Metrics to Look for

Liquidity Metrics to Measure Against (Moderate Private University*, 2019)

| | | |
|---|---|---|
| - Days Cash on Hand | **326** | (Liquidity X 365 /Operating Exp less Deprec) |
| - Operating Margin | **3.2%** | (Net operating revenue/Operating Revenue) |
| - Annual Debt Service Coverage | **2.76** | (Operating surplus+Depr+Int+Noncash Exp divided by principal & Interest) |

*Source: Moody's Investors Service, Higher Education – U.S. Medians, Private Universities have enrollment between 3,000 & 10,000 & less than 15% of revenue from Patient Care. Sample is 231 rated institutions including 17 below the Baa category.

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# **Making the Pivot**: Getting the Focus Right

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# Making the Pivot: Getting the Focus Right

In too many cases, the challenges of enrollment disruption [after 2025] will be layered on top of long-standing structural deficit problems

# Having the Right Tools

**Three key areas of analysis needed**

- Academic Program Margin Analysis
- Market Analysis for Academic Programs
- Modeling

**Approaches that work**

- Multidiscipline (Administrators & Academics)
- Collaborative
- Data Informed

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# Is This "Right Tools" Mantra Relevant?

| Survey Statement | Percentage Agreeing with Statement |
|---|---|
| At my college, we have the right mindset to respond quickly to needed changes | 68% |
| **At my college, we have the right tools & processes to respond quickly to needed changes** | 50% |
| **A lack of adequate data & analytic capacity is a significant obstacle to a sustainable financial future for my institution** | 44% |

Source: Inside Higher Education Survey of College and University Business Officers, July 2021, Pg. 27

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# Lessons from Observing Colleges – Leadership

1. **It all starts with leadership** from the board & President. Updating strategic initiatives considering current issues is the place to start, followed closely by the quantitative items below. What are your **habits & practices to monitor program demand**? Do you **maintain policy guardrails (like a net income or margin requirement)** that will encourage all leaders to make good choices about fiscal stability & academic quality? Are you **actively assessing collaboration &/or merger ideas?** The best merger & collaboration solutions come in times of financial stability rather than when a school is painted into a fiscal corner
2. Provide **strong programs with adequate funding** to keep them strong
3. **Prevent mission creep** by making sure only necessary programs are funded (even ones that are under-enrolled but deemed mission critical)
4. Be **proactive in finding alternative revenue sources** in academic programs & in the use of facilities & other assets such as intellectual capital. A growing number of schools have revenue committees at either the administrative level, the board level, or both

Provide stretch goals for advancement leaders. We are in the middle of a generational wealth shift that can be taken advantage of with the right emphasis & approach

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# Lessons from Observing Colleges – Quantitative

1. **Bend the administrative cost curve down**. This may prove challenging in an inflationary environment
2. **Bring academic program delivery cost in line** to reduce unnecessary costs using program revenue & cost analysis
3. **Rethink & reposition liquidity** to ensure there is adequate funding available in the downcycles that are inevitable
4. **Restructure debt, when possible,** to free up capital
5. **Forecast, measure results, & adjust**. A good modeling tool will help. Good budgeting tools also help but start with modeling to stay focused on the big picture

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# QUESTIONS

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