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POLICY BRIEF

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# COVID-19: Challenges for Higher Education

By Douglas Webber
Department of Economics, Temple University

## Highlights

- U.S. Higher education faces unprecedented financial challenges as a result of the ongoing pandemic.
- All aspects of university budgeting will be impacted. Less-selective public institutions are likely to be hardest hit.
- Federal stimulus is needed for the sector in order to ensure the health and finances of current students, and to protect the opportunities that higher education affords for future students.

U.S. higher education faces an unprecedented challenge from the COVID-19 pandemic which has upended nearly every aspect of daily life. In this brief, I detail some of the key financial challenges that institutions, particularly those in the public sector, will face in the years to come.

Before I begin, let's start off by stating that the first duty of any university to students, faculty, and staff must be to provide a safe environment to learn and work. Institutions of higher education will be unable to function without confidence from all parties that the college has an adequate plan and necessary resources to prevent outbreaks.

So why should the impending recession be any different than past economic downturns for higher education? We can break things down into factors which relate to expenditures and revenues.

### Expenditures

For colleges that offer some sort of on-campus instruction, the costs associated with simply providing a safe environment (testing, tracing, protective equipment) will be substantial. More importantly, there is no reason to expect any cost savings for schools that switch to online instruction. Quality online education costs at least as much to provide as on-campus instruction (Hemelt and Stange, 2020), and since most schools are in the midst of dramatically ramping up their online infrastructure they will face more immediate expenses relative to the few who have a mature online ecosystem (e.g. Western Governors University, an online university founded in 1997).

To be clear, there are certainly marginal reductions in spending that colleges can make; travel budgets seem unlikely to be needed in the coming year. The reality though is that most schools are not flush with cash or luxuries that can easily be cut. While the popular press tends to focus on the Ivy League or similar schools, such universities are highly unrepresentative of higher education as a whole (less than 1% of students attend an Ivy). The typical student attends either a community college or a non-selective public school with little that could be called “excess” spending. Selective private schools and state flagships will be able to cut their spending by (roughly) 5% with no discernible drop in education quality. This is not true for the majority of schools, where that magnitude of cut will likely be visible to students, and based on research will hurt both academic (Webber and Ehrenberg, 2010) and labor market (Griffith and Rask, 2016) outcomes.

## Revenues

The largest strain on university budgets in the years going forward will almost certainly occur on the revenue side of the ledger. The most immediate concern is that institutions will see a significant decline in tuition revenue. It is necessary to break down this revenue source into enrollment and tuition paid per student. Regarding enrollments (number of students taking classes), the coming academic year is uncertain as students wait to see what the college experience will look like in the age of COVID-19. Students may elect to sit out a year due to an underwhelming campus environment (with social distancing replacing social events) or a desire to put off coursework until it is face-to-face again.

There is a strong counterbalance to this downward enrollment pressure: opportunity costs. Enrollments in recessions typically increase since good jobs are harder to find. Given the depth and breadth of the current recession and its effect on the labor market, enrollments should not be a problem once the public health threat is controlled (e.g. a vaccine or highly effective treatment), and may not even be appreciably down in the coming year.

Despite this reality for enrollment figures, overall tuition revenue at many schools is likely to take a significant hit. First, out-of-state students (and especially international students) tend to pay higher tuition rates than local students. Given the nature of the pandemic, it appears likely that even if students do enroll in college, they will do so closer to home in order to avoid travel (and if possible may even continue to live at home). For international students, this issue is compounded further by ongoing barriers erected by the Trump administration. Typically, more affluent out-of-state and international students have been an important source of revenue for many public institutions seeking to make up for funding previously lost from declining state appropriations (Bound et al, 2020). Reductions in out-of-state enrollment are likely to persist for both the short and medium terms (if you start out in-state you probably won’t transfer out-of-state for your later college years even if public health concerns are alleviated). The decline in international students is likely a more permanent trend that will be exacerbated (but not caused) by the pandemic. It is important to note that at nearly all colleges out-of-state and international students should not be thought of as displacing local and domestic students. Instead, their higher tuition bills allow schools to admit more local and domestic students.

In the typical recession, state funding for higher education is displaced in favor of more immediate spending needs (similar to pension spending, higher education is a long-term investment), a prior analysis of mine on recession spending found much of the state support for higher education has gone to Medicaid expenditures for example (Webber, 2018). In the subsequent recovery, it is only partially replenished. Thus, there has been a downward trend in per-student state funding over the past several decades. As of this writing, most states are projecting budget shortfalls for FY20 of 5%-10%, and FY21 of 10-15% (National Conference of State Legislatures, 2020). Given this looming budget apocalypse that local and state budgets are facing, cuts will almost certainly be deeper than ever before.

Another area of significant revenue loss for most four-year institutions relates to on-campus operations like dorms, food, and parking. The best-case scenario for the coming year appears to be 50% dorm occupancy. Operational costs will likely not decline despite reduced occupancy due to costly safety measures that dormitories, dining halls, and similar facilities will need to incorporate. Operating these facilities was a previously stable source of revenue counted upon in university budgets. Thus, the budgetary impact of reduced operations will be very large. This is in addition to shortfalls already incurred last year due to housing refunds (at schools which could afford them) which cost many schools tens of millions of dollars.

While the above-mentioned declines in revenue sources are the most representative of what schools will face, select institutions may face unique budget problems. Universities with hospital affiliations (e.g. those with medical schools) will be hit hard as healthcare centers are also facing budget crises. And since college football generates the overwhelming majority of revenue for athletics departments, schools will likely be forced to significantly downsize these departments (both in per-sport support and the number of sports offered). And these are not simply temporary cuts either. Given the size of the shortfall (e.g. Wisconsin-Madison estimates a $100 million loss in revenue due to football alone) and the uncertainty about when things will return to normal, these cuts will likely persist long into the future.

## Policy Responses

The stimulus money distributed through the CARES Act was a necessary first step, but providing a safety net for individuals and preserving our economic system throughout the pandemic will take much more government action.

At a minimum, states and localities will require significant funding from the federal government. They do not have the luxury of being able to run deficits in tough times as can be done with the federal budget. While some refer to this as a "bailout", I want to make clear that states' budget problems are no fault of their own, the costs and loss of revenue spurred by the ongoing pandemic are unprecedented.

Universities, particularly large public institutions, are economic engines for both society as a whole and their local communities. They not only serve to build the skills which will power our economy in future decades, but each institution provides thousands of good jobs today. They are a critical part of our infrastructure. Federal support to states and local governments would provide the necessary stabilization for public institutions to make it through the current crisis.

I want to make a distinction between short-term liquidity problems and long-term solvency within higher education. The pandemic has created liquidity problems at many institutions, they lack the funds to operate at full capacity due to unexpected revenue losses, but in the long run (if funded) are still able to provide valuable labor market outcomes to students which justifies the public investment. This is distinct from solvency concerns, where an institution was struggling even before the pandemic and does not appear to provide the outcomes necessary to justify students' tuition and taxpayer investment. It is absolutely critical that we support any institution which is experiencing liquidity constraints but has no long-term solvency concerns.

Every year, a small number of (often very small private) colleges close or merge due to solvency problems in the same way that businesses fail every day. This is fine and can actually be healthy. Frameworks such as that proposed by the Federal Reserve system to provide credit to nonprofit entities through their Main Street Lending Program (Board of Governors of the Federal Reserve System, 2020) are an excellent way to ease liquidity problems while not using precious resources on a school which has no long-term future.

## Concluding Remarks

U.S. higher education faces an unprecedented financial challenge due to the ongoing pandemic. The magnitude of this challenge in the near-term is massive, and for some schools may even be existential. This will not be short-lived, as the coming recession will impact university budgets (especially among public institutions) for years to come. It is absolutely critical that the federal government provide support to universities as part of a larger package to help state and local governments. Not doing so would do irreparable harm to the many cities which count on universities as a local economic engine, the students (both current and future) who depend on the security and opportunities afforded by higher education, and the nation as a whole which depends on the sector for future economic growth.

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