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## For-Profit Higher Education: Godzilla or Chicken Little?

Gordon C. Winston<sup>\*</sup>  
Williams College

The issue is for-profit higher education. Not the Mom and Pop trade schools that have been around for a long time – beauty and secretarial schools and certification for truck drivers and diesel mechanics. It's the *accredited, degree-granting*, for-profit institutions like (of course) the University of Phoenix with 60,000 students and 1997 profits of \$33 million and DeVry, Inc. with 48,000 students and \$24 million in profits and ITT, Education Management, and Strayer Education, Inc. with 26,000, 19,000, and 10,000 students, respectively. These are glamour stocks on NASDAQ, rivaling internet companies.<sup>1</sup> Phoenix's price/earnings ratio was 50 last time I looked.

They're getting lots of attention. It is clearly fed by the nation's disenchantment with traditional colleges and universities and its infatuation with "privatization" and "the market." These schools, it is suggested, will harness the limitless powers of free enterprise to mend a failed higher education institution stuck in the past. But there's

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<sup>1</sup> A very nice article by Kim Strosnider in the Chron (1998) gave an overview of the sector and the results of a survey of the internet were reported by Ted Marchese (1998). See, too, Fischetti, et al. (1998). Arthur Levine's and Martin Trow's pieces (1997) in *Daedelus* do much to put it all in perspective.

more to it than unrealistic hype. So the issue is also how seriously to take this phenomenon – is it Godzilla, about to trample higher education, or are we just hearing the overwrought voice of Chicken Little? Or – a little less extreme – who’s vulnerable to this competition and why?

### I. The Economics of Entry

The vision – or specter – is simple. New information technologies and the organizational efficiencies of privatization can lower the cost of producing higher education enough that for-profit schools can compete with existing non-profit and public colleges and universities by offering students a better deal and still make a profit. Or they’ll produce an education that students deem more appropriate, improving quality from the consumer’s point of view. So, costs and prices will be lower or the education will be better, or both.

These characteristics of lower costs and differentiated product are amply evident in the new proprietary sector. The most has been written about the University of Phoenix, so it’s the easiest example.<sup>2</sup> Phoenix teaches its 60,000 students with a total of 45 full-time faculty members (up from 26 because of worries about re-accreditation) – and 4,500 adjuncts. Their libraries have no books – only journals and magazines available on-line. They operate in industrial locations and shopping malls rather than lovely parks. And it’s not just that cost and price are lower,<sup>3</sup> they make substitute products that are more appealing to significant parts of the market – Phoenix focuses

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<sup>2</sup> The facts that follow come largely from Marchese (1998) and Strosnider, (1997).

<sup>3</sup> The Strosnider (1997) reports that their price is between those of the public and private sectors.

explicitly on working adults (if you're under 23, you have to get special permission to take their courses) with subjects, time-of-day (and Sundays), and course locations tailored to those students and centrally written course syllabi that stress concrete, rather than abstract, learning (as recently praised by their 55 year-old student commencement speaker).

Economically, it looks like a classic case of market entry – right out of an undergraduate micro theory or industrial organization course. Price less average cost equals unit profit. If a new firm's costs and price can be lower than those of existing firms, it can make a profit in that industry, attracting customers by price. Or, if the new firm can produce a product the customers like better, it lures them away from existing firms by product qualities.

### *Entry into Higher Education*

But in higher education, there's a serious hitch in that familiar scenario. The structure of higher education is importantly unconventional in ways that have real implications for entry.

Looking at the cost-price-subsidy-hierarchy structure of higher education, reveals a set of facts that are very unusual in industry and very unfamiliar to, and even inconsistent with, our intuition [Winston-Yen (1995) and Winston (1999)]. In higher education:

- 1 – **Price is always less than cost.**
- 2 – The difference is made up by “**donative resources**” – from appropriations, gifts, endowment, and physical wealth.
- 3 – That is not a transient condition, but a **stable equilibrium**.
- 4 – So each student-customer gets a **subsidy**,  $s = c - p_n$ , as net price is less than cost.
- 5 – Those **subsidies are ubiquitous** within the industry.
- 6 – Individual schools’ **donative wealth** – hence their ability to subsidize their students – is **very different** among the 3,300 US institutions.
- 7 – So higher education is a sharply **hierarchical industry** in which cost, price, and subsidies vary dramatically among schools.

Table 1 summarizes these characteristics as revealed in 1995 IPEDS data.<sup>4</sup>

I'll resist the temptation to say an awful lot about these figures, since I've done that frequently in the past. But a few facts deserve emphasis. For the average non-profit college and university in the US, the subsidy per student is \$8,800 – an education that costs \$12,500 to produce is sold to the student for a price of \$3,700. That's the average. And public and private schools, I think surprisingly, give their students very much the same average subsidy -- \$8,917 in the public sector and \$8,673 in the private sector – only \$234 different. But those similar subsidies are the result of very different cost and

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<sup>4</sup> This is a bit different from similar tables published in earlier papers since it, appropriately for the present issue, eliminates all proprietary schools from the population of degree-granting institutions. [Winston-Yen (1995), Winston (1997)]

**Table 1**  
**Costs, Prices, Subsidies, & Hierarchy**  
**Non-profit Institutions by**  
**Control & Subsidy Decile**

	Subsidy (1)	Educational Spending (2)	Net Tuition (3)	Price to Cost Ratio (4)
	\$/FTE	\$/FTE	\$/FTE	%
<b>All Institutions</b>	<b>8,807</b>	<b>12,483</b>	<b>3,676</b>	<b>29.5%</b>
<b>All Private</b>	<b>8,673</b>	<b>15,312</b>	<b>6,639</b>	<b>43.4%</b>
<b>All Public</b>	<b>8,917</b>	<b>10,150</b>	<b>1,233</b>	<b>12.2%</b>
Decile 1	24,112	29,894	5,782	19.3%
Decile 2	11,765	15,747	3,982	25.3%
Decile 3	9,768	12,966	3,198	24.7%
Decile 4	8,603	11,297	2,694	23.8%
Decile 5	7,728	10,444	2,716	26.0%
Decile 6	6,940	9,800	2,860	29.2%
Decile 7	6,235	9,179	2,944	32.1%
Decile 8	5,535	8,658	3,123	36.1%
Decile 9	4,702	8,357	3,656	43.7%
Decile 10	2,620	8,419	5,799	68.9%

Source: IPEDS data in Winston-Yen, (1995), updated.

N = 2591

price policies – in the public sector, a \$10,150 education is sold for a price of \$1,230 while in the private sector, a \$15,310 education is sold for \$6,640. Average expenditures are half again as large as in the private sector but their average price in the private sector is six times higher!

The real meat of Table 1, though, is in the decile rankings that separate schools by the size of their student subsidies. Even in these crude averages – lumping public and

private schools together – the range is impressive. From bottom to top deciles, average subsidies increase by a factor of almost ten, from \$2,600 to \$24,000. It's interesting, though, that expenditures per student aren't nearly as different – they range only from \$8,400 to just under \$30,000 at the top. That means, of course, that the net price the average student pays is even less differentiated – indeed, students in the bottom decile schools actually *pay more* in net tuition, on average, than those in the top decile; \$5,800 against \$5,780.<sup>5</sup> Net price is U-shaped, going down the hierarchy, bottoming out in the fourth decile and rising monotonically below that. Finally, a price-cost ratio organizes these same facts a bit differently, showing that the price paid by students in the top decile covers less than 20% of their educational costs – twenty cents on the dollar – while students at the bottom pay nearly 70% of their costs.

### Profits and Subsidies

What does this mean for entry into such an industry by for-profit firms? The most important implications are, I think, pretty obvious. For any firm,

$$\text{unit profit} = \text{price} - \text{cost}.$$

But we've just seen that in the typical college or university,

$$\text{student subsidy} = \text{cost} - \text{price}.$$

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<sup>5</sup> That's probably making more of the data than they can support, but even if the \$20 difference isn't significant, it is quite significant that they are close.

So they're exactly the same thing with different sign: subsidy is simply negative profit; profit is negative subsidy.<sup>6</sup>

So a school's student subsidy shows how much an entering school would have to lower costs in order to compete with it on cost and price, nose to nose, and still make a profit. Since the average college or university in the US gives each student an \$8,807 a year subsidy, the per-student educational costs of an entering firm competing strictly on price – producing exactly the same kind of education – would have to be at least \$8,807 lower. The price-cost ratio puts this a bit differently: the entering firm would have to reduce costs – relative to the established college – by  $1 - P/C$  or, for the average US school, by more than 70 percent.

### Subsidies as Barriers to Entry

A school's *student subsidies are a barrier to entry*. They describe the minimum cost reduction necessary for an entering firm to compete with the existing school at a competitive price and still make an economic profit. They are, note, also a barrier to entry for, or to effective competition from, other non-profit schools, farther down the hierarchy.

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<sup>6</sup> The distinction between “economic profits” (recognizing capital costs) and “accounting profits” (ignoring them) familiar to all Econ 101 teachers qualifies this statement. All subsidy calculations include capital service costs as a rental rate so subsidies are the negative of *economic* profits. For-profit conventions deal in accounting profits, neglecting capital costs, so it should be noted that a return of 8.44% to capital is built into the figures and discussion, on top of conventional accounting profits. A back of the envelope adjustment along the lines of our IPEDS calculations [Winston-Lewis (1997)] for the profits of Phoenix and DeVry leave them with smaller but still very positive economic profits.

And while the subsidy is least ambiguous as a measure of protection from pure cost-reduction competition – of the sort sometimes touted for high-tech education – the subsidy is also an indication, if less precisely, of what kind of barrier an innovative new entrant with a different kind of education would have to overcome – how much better students would have to view that school’s product in order to feel they were getting as good a deal as from the traditional school. Subsidy, then, reflects the height of the barrier any entering firm will have to overcome, one way or the other.

## II. The Vulnerable Schools

So, inverted, a table of subsidy values becomes a “Table of Vulnerability,” an identification of those schools with small student subsidy resources that can therefore most easily be picked off by for-profit competition.

This is made more explicit in Table 2 where the low-subsidy schools are divided by Carnegie type and public or private control to give a picture of what kinds of schools are most vulnerable to for-profit competition. In the first section are the 259 schools with the lowest student subsidies – those in the tenth decile of Table 1 – while those in the second section are the 777 schools with low subsidies – the bottom three deciles of that table.

The schools least able to withstand for-profit competition, clearly, are concentrated in the private sector – more than four out of five are private and within that group, the largest number – 66 – are comprehensive universities. Private specialized

Table 2

**Vulnerability  
to For-Profit Competition**

**I. The Most Vulnerable - Lowest 10% of Subsidies**

	<i>Number of schools by type and control</i>		<i>As percent of type and control in population</i>	
	<u>Public</u>	<u>Private</u>	<u>Public</u>	<u>Private</u>
Research	0	1	0%	3%
Doctoral	1	12	2%	28%
Comprehensive	5	66	2%	27%
Liberal Arts	4	49	5%	9%
Two-year	32	38	4%	32%
Specialized	0	51	0%	25%
Total	42	217	3%	19%

**II. The Vulnerable - Lowest 30% of Subsidies**

	<i>Number of schools by type and control</i>		<i>As percent of type and control in population</i>	
	<u>Public</u>	<u>Private</u>	<u>Public</u>	<u>Private</u>
Research	4	2	5%	5%
Doctoral	10	18	16%	42%
Comprehensive	42	141	15%	58%
Liberal Arts	18	133	23%	26%
Two-year	263	59	30%	49%
Specialized	1	86	2%	42%
Total	338	439	24%	37%

institutions<sup>7</sup> – with 51 – are next, followed by liberal arts colleges – 49 – and private two-year colleges – 38. Only one private research university shows up as highly vulnerable (and that could easily be a data fluke since there are lots of them when IPEDS data are used for a single school). Among public institutions, the only type that comes close is two-year colleges, of which 32 are in the highly vulnerable category.

But it's more meaningful to put these numbers in context by showing the highly vulnerable schools as a percent of each type-control category in the whole population. This is done in the last columns. So with a total of 120 private two-year colleges in our data, 32 percent of them are in the bottom subsidy decile, as are 28 percent of private doctoral and 27 percent of private comprehensive universities, 25 percent of private specialized schools, 10 percent of private liberal arts colleges and 3 percent of private research universities.

Very few public sector schools appear to be highly vulnerable – only 3 percent of them – and while three out of four of these are two-year colleges, even those 32 schools represent only 4 percent of the 874 public two-year institutions in the data.

The lower section of Table 2 describes the vulnerable 30 percent of the colleges and universities – the bottom three subsidy deciles – tells much the same story if one

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<sup>7</sup> A word on the “specialized institutions” in Tables 1 and 2. Behind the data are important differences in the kinds of schools that fall into that category between public and private sectors. In the private sector, the 203 specialized non-profit institutions in our population are largely religious (41%), business (17%), and art schools (21%) while in the public sector, the 50 specialized institutions are concentrated in health care (32%) and tribal schools (28%) – public medical schools often have enough undergraduates to have made it into our population. Hence the very different cost, price, and subsidy data for specialized institutions in the two sectors. See

moderated by including a larger proportion of public institutions (56 percent) mainly as two-year and comprehensive schools. Even so, only a small percent of public institutions have subsidies so low as to put them in this vulnerable category -- 5 percent of public research, 16 percent of doctoral, and 15 percent of comprehensive universities; 23 percent of public liberal arts and 30 percent of public two-year colleges. Only 2 percent of public specialized institutions have such low subsidies. So all public institutions are equally- or under-represented in these three deciles.

But the much greater vulnerability within the private sector is amply evident, once again. The bottom three deciles include fully 58 percent of private comprehensive and 42 percent of private doctoral universities, 49 percent of the two-year colleges, and 42 percent of private specialized institutions. Only private research universities (5 percent) and liberal arts colleges (26 percent) are under-represented in this low-subsidy third of the population.

It could be argued, persuasively I think, that this approach is far too aggregated – that whether a school is vulnerable depends crucially on what, exactly, it's doing and whether that kind of education can be produced more efficiently with a different technology or organization – it's not just a simple matter of the arithmetic of subsidies and profits. And that's true. But what makes that a less damaging criticism than it might be is that these low-subsidy schools, in search of enrollments, have already moved into those practical, concrete, occupational-vocational curricula [Breneman (1994), Winston

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Winston-Yen (1995) for the details of generation of the population from the IPEDS data, but one criterion was that 20% of the students be undergraduates.

(1999), and Trow (1997)] that appear least protected from the new competition – “training,” more than “education.” And they’ve done it, by and large, with the old, conventional, methods.<sup>8</sup>

### What Happens to the Losers?

I don’t want to go very far on this tack, but it’s useful to ask what’s likely to happen to them – if the vulnerable private schools lose out to for-profit competition? Say that a non-profit school is pushed over the edge by the aggressive for-profit competitor that can cut costs or tailor its education successfully enough to take the market away? In other words, what’s “over the edge?” (Parenthetically, it’s useful to remember that a ‘tidal wave’ of enrollments is soon expected that may lift all boats for a while, even the very leaky ones, making this an important but perhaps not an immediate question.)

Two alternatives appear. One is that the non-profit school might fight back, making significant changes in what they do and how they do it, either to reduce costs or to alter their product and organization to meet the competition. If you can’t beat ‘em... That might mean altering the school’s relationship with its faculty – using fewer full-time tenured faculty and more part-time adjuncts and, if Phoenix is a guide, reducing faculty discretion over both what is taught and how it’s taught.<sup>9</sup> It might mean – as RPI, NYU,

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<sup>8</sup> Levine (1997): “...students are more likely to prefer concrete or practical subjects and active methods of learning while faculty are predisposed to abstract and theoretical subject matter and passive methods of learning. The result ... is frustration on both sides ...and a tendency for faculty to interpret as deficiencies what may simply be natural differences in learning patterns. This mismatch may cause faculty to think every year that students are less and less well-prepared and for students to think their classes are incomprehensible.” (pp.8-9).

<sup>9</sup> Levine (1997, p.17): “What they [the new proprietary universities] will mean for faculty is a vastly different role, one that does not include participation in governance, and minimal activity in curriculum planning. The emphasis will be on increasing teaching productivity and eliminating scholarly expectations. Total salary costs will be lower, and all or most faculty will be part-time.”

BU, and others have shown – a more aggressive counterattack like one that capitalizes on an academic reputation to sell employee-education to major business firms, directly or electronically, meeting the for-profit firms on their own turf. Either way, the private non-profit school that chooses to compete would probably retain its donative wealth which would protect some, at least, of its procedures and values and curriculum from pure commercial pressures, even while its operations were very much affected by those pressures.<sup>10</sup>

The other alternative – taking a cue from the health care industry – is that the weakened non-profit school might well sell out to a for-profit firm. Or become one. And while that may sound very straightforward, it isn’t when you recognize that the distinguishing feature of a non-profit firm is that nobody owns it – it has no owners because of the “non-distribution constraint” that keeps it from distributing profits. So who negotiates its sell-out price on behalf of the vanishing school? And, more important, who gets paid the money?

The only hint I’ve come across on this is in a very nice *New York Times* piece on the sale of non-profit hospitals [Lewin with Gottlieb (1997)]. In that industry, it’s been presumed that the hospital “belonged,” in some sense, to the local community so the for-profit purchaser paid the purchase price to a local foundation that was set up to negotiate price, receive the money and, subsequently, to spend it on community-related services. There tends to be, predictably, a very fuzzy line between the buyer and the community

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<sup>10</sup> One can only speculate on what would happen to public support of an aggressive and successful public sector school – whether legislatures would withdraw tax support in light of their ability to earn private revenues or

foundation and its management and there are clear and strong incentives for the buyer to influence the price it has to pay and even the subsequent use of its funds. Applied to colleges, the only solace is that – as seems apparent from the data above – the schools most likely to be sold to for-profit firms are those with the least resources, a fact that limits the scope, if not the principle, of potential skullduggery.

But in the kind of broad survey Ted Marchese has recently done, “partnering” appears as a middle ground between these extremes – the cooperative association between aggressive for-profit firms and (aggressive?) non-profit schools in search of new markets and new sources of revenues. So Caliber (jointly owned by Sylvan and MCI, has cooperative agreements with Johns Hopkins and Wharton; The Western Governors web-based university has 14 partners including IBM, Sun, AT&T, KPMG, and Microsoft; and the University of Wisconsin has partnered with Lotus in a venture with for-profit and non-profit branches to sell Wisconsin courses and degrees worldwide. And so on. Note, importantly, that there is no absence of high-subsidy schools in this list, suggesting that the line between defensive reaction and energetic innovation is increasingly a fine and wobbly one.

### III. The High-Subsidy Schools

Are the high-subsidy schools at the top of the hierarchy impregnable? UVA and Williams and Duke and Yale and Swarthmore?

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reward them for their practical community service.

“Impregnable” is probably a bit strong, but they’re far more secure from the kind of survival pressures described so far, simply because their student subsidy barriers are so very high. In order to go nose to nose with Williams and still make some profit, a private firm would have, somehow, to overcome a \$40,000 a year subsidy per student, cutting educational costs by some 60% while maintaining quality. In equilibrium, not just to break into the market. The average private school in the top decile gives a subsidy of \$24,138 and has a price-cost ratio of 0.254. It’s not likely either that costs can be cut or product improved enough by an entering for-profit firm to turn a profit, especially since the high quality, residential liberal arts education these schools often produce is hand-crafted and appears highly dependent on peer interactions with other good students, so it is resistant to easy cost-cutting. And just what these schools actually sell is not well understood – as the many efforts of assessment groups have shown.

### Competition for Courses

But there seems to be a more subtle threat to these schools in the form of for-profit “functional cherry-picking” – for-profit firms’ competing with the high-subsidy school for part of what it does. Sharon Oster [1997] has done a very nice paper on the characteristics of institutional activities that make that kind of incremental for-profit entry attractive. She did it from the other end, asking about the characteristics of the activities that a non-profit university might choose to contract-out, but it’s the same question, except for who takes the initiative. From the university’s side, it’s old hat: Saga and Marriot have long been supplying food services; Barnes and Nobel is a major operator of

campus bookstores; ServiceMaster is a widely used contractor for maintenance and janitorial services, and so on.

The new pressure that for-profit education adds is on the *curriculum* – the “core mission” in Oster’s phrase – and with it come immediate questions of university control and ownership of intellectual property – most fundamentally, what it is that the high-subsidy college or university sells. These are not questions that appear to have got a lot of serious attention – their answers may have seemed both obvious and elusive.

But if for-profit schools start competing for those *parts* of a curriculum – those courses and programs – on which they can make a profit, the whole argument about vulnerability above – about identifying vulnerable institutions by the size of their student subsidies – would be repeated *within* the high-subsidy schools’ curricula to identify vulnerable programs and courses. Even the school that gives its students a \$50,000 a year subsidy will have some courses and even whole programs maybe where student subsidies are much smaller, or even negative.<sup>11</sup> Or courses and programs amenable to significant technological cost-reduction.

Oster’s construct is useful in this context, too. She identified two key dimensions of a university activity: the *complexity* of its goals and whether it is amenable to *scale economies*. Those activities that are complex and have no scale economies in production are the natural stuff of the non-profit; those that have significant scale economies and are

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<sup>11</sup> Different subsidies by function, of course, were identified by Estelle James (1978) twenty years ago as the basis of her analyses of internal cross-subsidies.

simple to define and monitor are the stuff to be contracted-out to the large for-profit firm; activities that are small scale and simple are appropriate for contract to a small for-profit firm. The fourth kind of activity in the taxonomy – with complex goals but subject to scale economies – is a toss-up. And all this, she stresses, is set in a university environment in which management decisions have to be more explicitly political – balancing among stakeholders – than under for-profit organization. Trow (1997) describes some of these problems in the University of California system.

While Oster made it very clear that she meant her analysis to apply only to ancillary activities and support services – not the school’s core learning mission – the entry of for-profit schools into the curriculum of higher education breaches that convenient wall and when it does, her analysis seems relevant within the core activities, too. A university’s curricular offerings differ markedly among themselves in the complexity of their goals, from the concrete (even vocational) courses to the abstract stuff of the liberal arts. And courses differ, too, in their ability to benefit from scale economies – Marchese reports that for-profit firms are putting together high-tech distance learning courses at a budgeted cost of \$80,000 per instructional hour (so a one-semester course would cost \$2 million to construct and market), suggesting that someone expects very large scale. Indeed, Oster’s two dimensions, applied to a curriculum, seem to parallel the distinction that Bill Pulleyman – the head of IBM’s Math Department – made between the company’s internal “training” and its internal “educational” activities (with the significant fact that IBM sees only the first of these as amenable to high-tech methods) [quoted in Roberts (1998)]. High-subsidy colleges and universities do a lot of “training”

and Breneman's study of Liberal Arts colleges (1994) suggests that they may have been doing more and more of it over time. And – to add one more nail – Hansmann has recently (1996) noted that government certification and licensing of complex things like educational programs and courses and their outcomes reduces the need for the buyers' trust that is the key transactional element provided by non-profit organization.

So if a highly TA-dependent accounting course, for instance, were one of a university's profitable offerings, a for-profit school in a shopping mall on the outskirts of town – or one entering the internet from Omaha or Osaka – might offer a better-taught course or a lower price. Of course, the university has to be willing to accept "transfer credits" in order for that competition to apply toward the university's degree, but if it refused to do so, simply because those credits were from a for-profit school, that would raise all sorts of awkward issues – the role of Advanced Placement test credits and proficiency exams in areas like French and basic mathematics. And "partnering," again, means that such credits will increasingly come from schools with unexceptionable academic credentials like Wisconsin and Duke and NYU. "...[A]ll institutions, Ivies and medallions included, may see their undergraduate franchise eroded as enrolled students appear in the registrar's office with brand-name course credits taken over the Web." [Marchese (1998)]. Or at the mall. The local political elements of such a prospect might be quite difficult to sort out [see Oster (1997) and, especially, Trow (1997)]. And it may be reasonable to expect that competition among non-profit schools in these dimensions would tend to erode what resolve any traditional school might have to resist.

Such systematic cherry picking – competition for profitable parts of a curriculum – would have serious effects on the university’s ability to do what it’s been doing by reducing its ability to cross-subsidize activities – to support the Classics Department with “profits” from Accounting. Which goes back, again, to the underlying question “What do traditional colleges and universities sell?” Is it a degree? Screening? A series of courses? Certification of achievements? A learning experience? A social experience? Peer bonding? These won’t be easy things to disentangle, especially under pressure of aggressive market competition and complicated stakeholder politics.<sup>12</sup>

So it seems that rather than being able to remain aloof and unaffected by for-profit competition – or enter the arena on their own terms – high-subsidy schools will, at the very least, have to know much more about the costs of their curricula – to do a subsidy-by-course analysis of the sort done by school above – and think much more carefully about what it is they’re selling and who’s going to be allowed to produce its component parts.

### III. Godzilla?

What can we take from all this? I think, broadly, two things: first, that the direct impact of for-profit competition will be very unevenly distributed among colleges, threatening the continued existence of only those schools with meager donative resources that give their students quite modest subsidies and, second, that wealthier, higher-subsidy

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<sup>12</sup> Bill Massy makes a compelling argument that it is just this distance from market-clearing, for-profit pressure – the subsidy in my terms – that allows higher education to be *higher* education. This is most conventionally framed in seeing large social externalities attached to the “less practical” and vocational curricula – to an educated polity – which suggest that its potential under-supply is now offset by public and private subsidies. [Massy]

schools will be forced to clarify what it is they sell, educationally, and who they will allow to produce it – raising sticky issues of intellectual property and ownership and governance and autonomy. Together, these will make for exciting times with real ramifications for the world we live in.

*Does Society Benefit?*

Let me end by skating onto even thinner ice to speculate briefly about whether this for-profit, privatized, competition is A Good Thing. Socially. Economists always have an uncomfortable time of it with the tension between what's good for Society and what's good for an individual firm or industry. “What's good for General Motors” is not always good for the Country, but the economist who makes a judgement on that may be a consultant to General Motors. When it's the firm and the industry that we work in, that conflict doesn't become any easier to resolve.

I'd conclude that there's a whole lot of overstatement in all this about what high-tech for-profit competition is going to do to colleges and universities – Peter Drucker's famous prediction that in thirty years, the university as we've known it won't exist [quoted by Lenzer and Johnson (1997)]. There's a lot of Buck Rogers and Luke Skywalker in recent comments on higher education – a technological ebullience reminiscent of the days of sweeping engineering projects like Grand Coulee and Hoover Dams, reinforced this time by the privatization romance.

But despite overstatement, these appear to be sources of very real change. “Higher education” has come to include an astonishingly large part of the US population without, it seems to me,<sup>13</sup> an entirely realistic recognition of the heterogeneity of that larger population in their needs, interests, abilities. That’s the demand side. On the supply side, administrators, legislatures, trustees, and (maybe especially) faculties seem too often to be guided by emulation of the schools and attitudes and techniques that are appropriate to the top. US higher education institutions have tended to be Harvard-in-the-small, with the assumption that what works for the students and the faculty on top of the hierarchy – or something much like it – is appropriate for those who are serving very different students with very different interests and needs. Abstractions and first principles *are* “higher education.” It may feel egalitarian to take the position that everyone deserves the best, it seems often to have been unrealistic, producing a product that many of our customers simply don’t much want to buy<sup>14</sup>.

If that’s right, what’s coming, driven by the for-profit sector, is a sharper differentiation of product with a greater variety of educational choices to match the greater variety of educational needs and interests inherent in a radically expanded and more heterogeneous student population. Levine calls it “a Boutique-ing” of higher education (1997, p.3).

I think that addresses much of the “Is It A Good Thing?” question. Socially, for-profit competition will do what privatization is supposed to do – push toward a wider

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<sup>13</sup> And to Marchese (1998) and Levine (1997), among others.

<sup>14</sup> See again the Levine quote in n. 8, above.

range of products at lower costs and the elimination of inefficient and inappropriate schools. While the new information technologies may play a significant role in that push, as large part of it, I suspect, will come from the break with emulated traditions – like reliance on full-time tenured faculty, faculty governance and curricular freedom – that have trickled down the hierarchy of traditional schools but come under increasing pressure from the bottom of that hierarchy when firms are trying to make a profit. And the competition will not only replace many of the vulnerable schools, but forever alter the products and processes of those that successfully resist it.

The wealthy schools giving large student subsidies and expensive, traditional, residential educations that capitalize on peer quality will remain in the niche market they've always been in but with a clearer sense of what they are, what they do, and what role an aggressive for-profit sector should play in doing it. Those selective schools will continue to attract students through their high subsidies and continue to provide the externalities of an educated citizenry through an “impractical” higher education – but they will appeal to a small and very different segment of society than the for-profit schools that give the rewards of immediate and concrete training.

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