



**TIAA-CREF** institute

# Financing Institutional Operations The Entrepreneurial Leader

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# Our “industry”

## Positive:

- Large and Growing
  - Student growth (1994-2004): 1.9% Compounded Annual Growth Rate (CAGR)
  - Number of institutions (1994-2004): 1.6% CAGR
  - Research (1993-2003): 5.0% CAGR, inflation adjusted
  - Faculty numbers (1987-2003): 2.3% CAGR
- Diverse types of institutions
- Reputation world-wide
  - Number of US institutions in top 10: 7 or 8
  - Number of US institutions in top 50: 20 or 37
  - Number of US institutions in top 200: 54 or 87

Note: Some data in this presentation are drawn from a paper presented by Paul Jansen, McKinsey & Co. at the Forum for the future of Higher Education, September, 2006



## Our “industry” (continued)

- Diverse funding
  - Government (Local, State and Federal)
  - Tuition
  - Philanthropy
    - Total philanthropy: 107% increase in 20 years
    - Higher share of total US philanthropy: 170% increase in 20 years
- Tax-advantaged treatment by Government
  - Access to tax exempt capital markets
  - Investment earnings untaxed
  - Favorable tax treatment for donors



# Challenges?

- Short term (perhaps 10 years) revenue challenges
  - Generally, diminished Government spending
    - State and local funding adjusted for numbers of students and inflation going down
    - Federal research funding declining when adjusted for inflation
  - Growth of tuition, net of institutional financial aid, is likely to be restrained
  - Philanthropy, positive totals, but more and more targeted



## Challenges? (continued)

- Longer term
  - Rich are getting richer
    - Growth (1999-2005) in top 10 university endowments equal to the increase for the next 90 largest
    - Student demand very strong at the “elite” institutions
    - Intellectual property pay-offs: can be very large, but concentrated in just a few institutions
  - Educational world is flattening
    - Fewer international students coming to and staying in the US
    - Large investments in higher education in developing countries
    - US institutions exporting programs internationally
  - Pressure on revenue sources



## Macro-economics of “Industry”

- U.S. economy: Productivity in private-goods industry is up
  - More than 2.5% since 1977
  - 3.5%, 2000-03
- Basic higher education delivery model, except perhaps limited internet, unchanged for decades
- Overall productivity loss in higher education:
  - Growing overhead
  - More regulation and mandates
  - Inflation adjusted salaries of full time instructional faculty are up (1985-2005)
    - Private four year: 3.7% (CAGR)
    - Public four year: 3.2% (CAGR)
  - Increase in administrative costs per student (1984-2004): 54% adjusted for inflation

## Infrastructure constraints

- Heavily capital intensive
  - “Arms race” for student amenities
  - Lake Woebegone effect on research goals
    - “Star” faculty salaries
    - Expensive buildings and equipment
- Not able to be nimble
  - Tenure and “tenure-like” status for staff
  - Heavy investment in facilities
  - Idiosyncratic business systems/processes
- Research not fully funded by Government sponsors

## What might the future look like?

- Further government regulation
  - Cap, or other restraints, on tuition increases
  - Loss of tax exempt advantages
- Favorable capital market performance may disappear
  - Higher cost of borrowing
  - Investment returns suppressed
  - Inflation
- Losing best students, particularly international, to other countries
- Expenses, including faculty salaries and facilities, continue to rise relative to inflation



# Possible entrepreneurial financial approaches

- Invest more heavily in administrative technologies
  - Really exploit ERP (Enterprise Resource Program) capabilities
    - While they are
      - Expensive to install
      - High initial outlays in training and business process change
    - They permit
      - Opportunity to engage in best administrative practices
      - Fewer, more sophisticated users
- New research models
  - Less duplication of expensive facilities
  - Just-in-time, limited life buildings
  - Ability to cut costs quickly
    - Lease space and equipment
    - “Tenure down” faculty

## Possible entrepreneurial financial approaches (continued)

- “Outsource” administrative applications
  - Why not?
    - “But we’re special”
    - “We’re too complicated”
    - “We cannot lose control”
  - Analysis: Suppose
    - Reduction of administrative costs by one third
    - Say administrative costs run 25%
    - 8% overall savings