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Why Does College Cost So Much?

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Increases in college tuition have long outpaced growth in family income—in effect, placing higher education out of reach for an increasing number of American families. Economic factors account for that trend, but also ensure that it cannot be sustained much longer.

As college students begin a new academic year, many parents are reeling from tuition charges. This fall's estimated 8 percent average increase at public universities, added onto double-digit hikes in the two previous years, means tuition at a typical state university is up 36 percent over 2002—at a time when consumer prices in general have risen less than 9 percent. In inflation-adjusted terms, tuition today is roughly triple what it was when parents of today's college students attended school in the 1970s. Tuition charges are rising faster than family incomes, an unsustainable trend in the long run. This holds true even when scholarships and financial aid are considered. One consequence of rising costs is that college enrollments are no longer increasing as much as before. Price-sensitive groups such as low-income students and minorities are missing out. A smaller proportion of Hispanics between eighteen and twenty-four attends college today than in 1976. The United States is beginning to fall below some other industrial nations in population-adjusted college attendance.

There are six factors in the cost explosion:

Rising Demand: The "natural" economic consequences of a rising demand—higher prices and a larger quantity consumed—are exacerbated by soaring third-party payments. Since 1994, financial-aid payments (mostly federal loans and grants) have risen by an extraordinary 11 percent per year. When someone else pays the bills, we become less sensitive to price.

Lack of Market Discipline: Most universities are nonprofit. There is no bottom line. Did Yale have a good year in 2004? Who knows? Its stock is not traded. Administrators and faculty are not rewarded for increasing profits by reducing costs or improving product quality. When prices rise in the for-profit sector, entrepreneurs rush to supply the good, leading to higher supply and lower prices. How many universities advertise that they are cheaper than their peers, or offer better value?

De-emphasizing Undergraduate Instruction: Data from the National Center for Education Statistics show that most colleges (but not community or liberal-arts colleges) have reduced the share of resources devoted to undergraduate teaching, spending more on other things—research, administration, student services (luxurious recreational and student centers), athletics, etc. Only about twenty-one cents of each new inflation-adjusted dollar per student since 1976 actually went for "instruction." Government subsidies and private gifts given to support affordable undergraduate instruction are often spent elsewhere.

Price Discrimination: Universities have discovered what airlines realized a generation ago—they

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increasingly charge the maximum that their different customers will bear. They have raised sticker prices, giving discounts (scholarships) to those who are sensitive to price. Increasingly, these discounts go not mainly to low-income students but to talented students prized by universities seeking to improve ratings on the athletic field or in the *U.S. News & World Report* rankings.

Stagnant (Falling?) Productivity: While measuring productivity in post-secondary education is difficult, the ratio of staff to students has risen over time. There are now six non-teaching professionals for every 100 students, up from three a generation ago. Unless teaching and research have soared in quantity and quality, which seems unlikely, productivity has fallen.

"Rent Seeking" Behavior: Better Lives for the Staff: Faculties have shared in the increased income of universities. Salaries of full professors at research universities are up well over 50 percent in real terms since 1980. Mid-six-digit salaries are becoming commonplace for superstar faculty, coaches, and university presidents. Teaching loads have fallen (a typical full professor at a major public university is in class no more than five hours per week).

What is the solution? New forms of competition (for example, for-profit institutions, online schooling, more use of community colleges, and new approaches to certifying skills) are emerging. State legislatures have sharply reduced their share of funding for public universities, forcing some schools to slash costs, reduce bureaucracies, increase teaching loads, get rid of costly underutilized graduate programs, and more. Some schools are talking of using buildings more than eight or nine months a year, or are cutting down on the use of expensive tenured faculty. Colorado is shifting funds away from institutions and into student hands in the form of vouchers, reasoning that the student-customer, not the producer, should be sovereign as in nearly every other transaction.

The cost of higher education cannot rise faster than incomes indefinitely. Change is coming: it is just a question of when, and in what form.