ENQUIRER ILLUSTRATION/RANDY MAZZOLA

COVER STORY

THE NEXT BUBBLE?

In 2013, The Enquirer explains the confusing and costly world of higher education. Today we examine an industry experts say is ripe for disruption, with consequences for students, parents, workers and the region's economy. Coming Monday: How online courses threaten higher ed's business model.

Internet bubble.

What inflated the bubble? The NASDAQ Index exploded to 5,000 in 2000 from 600 in 1996, as investors flocked to dot-com companies going public without earning any profits. Silicon Valley, the story went, created a new millionaire every 60 seconds.

What made it pop? Panic selling starting in early 2000 pushed the index back down to 800 as investors realized that some dot-com stocks were only ideas, not great companies. Scandals emerged showing that tech companies had artificially inflated their profits.

Who paid the price? Hundreds of thousands of technology workers lost their jobs, and investors caught up in the dot-com craze lost their life savings.

Housing bubble.

What inflated the bubble? A 90 percent increase in housing prices from 2000 to 2006, fueled by easy credit and low interest rates.

What made it pop? Speculators entered the market, delinquencies skyrocketed and prices collapsed to the point that they wouldn't support home mortgages.

Who paid the price? Home owners forced to default when who found themselves under water on mortgages, taxpayers forced to bail out failing banks.

College bubble?

What is inflating the bubble? Tuition at both public and private universities has more than doubled in the last 30 years, facilitated by government-guaranteed student loans.

What could make it pop? Families could desert colleges that cost too much, forcing a cash crunch at weaker universities. Government subsidies could dry up, and students borrowing for tuition could face higher costs.

Who could pay the price? Students with fewer options, employees of weaker universities, taxpayers forced to bail out borrowers and universities.

Education costs are out of control. In peril? Students, taxpayers and universities, plus the local economy that will take a hammer blow if the hometown school fails

The cycle keeps repeating itself, over and over.

College tuition keeps increasing, students keep borrowing – mainly from taxpayers – and universities keep spending.

Even college presidents acknowledge that they can't sustain the pattern and as families choose alternatives, the day of reckoning is coming.

Not just for families who can't afford tuition. The system itself is vulnerable, perhaps even inflating a financial bubble on the scale of the Internet bubble of the late 1990s or the housing bubble that helped crash the economy in 2008.

"Schools are going to go broke," Ohio University economist Richard Vedder said.

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"The weaker liberal arts colleges and the weaker state universities will suffer because they don't have a lot of money and a lot of outside support," Vedder said. "They're just simply going to go by the wayside."

Such a crash would hamstring universities, leave students with limited choices and debt they can't repay, and potentially force taxpayers to pick up the tab.

As Greater Cincinnati grows increasingly dependent on universities, any widespread pain for the region's schools would boomerang throughout the economy here.

Even after several years of shedding excess workers, higher education employs nearly 30,000 people in the region, both full-time and part-time, and the University of Cincinnati is the biggest single employer, with about 16,000 on the payroll.

But any disruption would radiate well beyond college campuses in University Heights, Highland Heights, Delhi Township or Oxford.

Entrepreneurs would find weaker support without research done in

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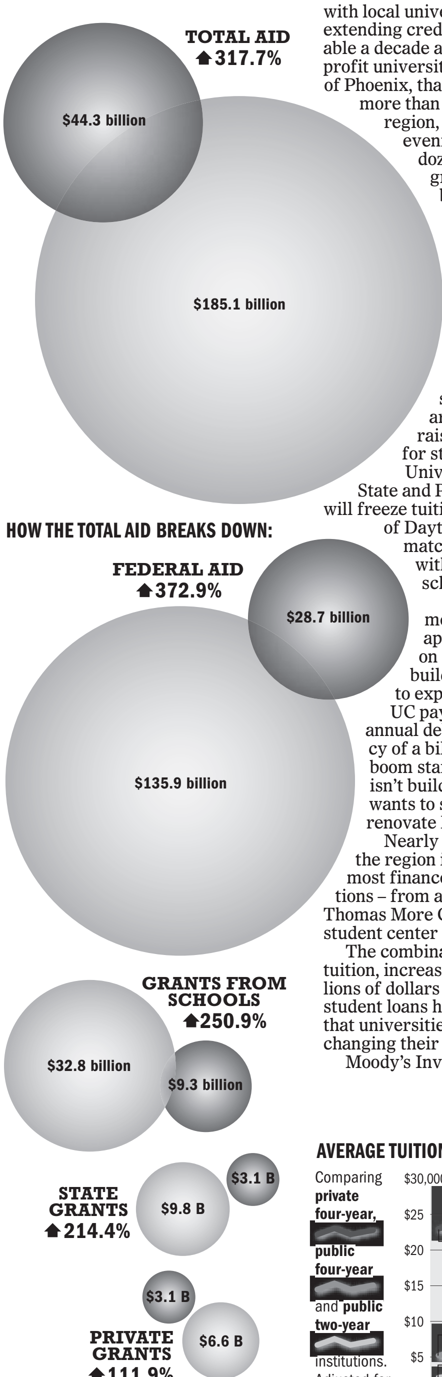
What's expanding the bubble

TOTAL UNDERGRADUATE STUDENT AID

Comparing the **1991-92 school year** to the **2011-12 school year** and the percent change of each category. Circle sizes represent amount of aid. Figures adjusted for inflation to 2011 dollars.



Source: College Board The Enquirer/Mike Nyerges

college labs and incubators. Fewer talented professionals would migrate to the region. Without the most consistent source of new buildings and big renovations, local architectural and construction firms would suffer.

Universities acknowledge that they must reign in spending and adjust to a new world where students can choose other options.

One alternative: Massive online courses offered by other vendors with local universities eventually extending credit, a concept unthinkable a decade ago. And another: For-profit universities, such as University of Phoenix, that collectively have more than 10,000 students in this region, offering convenient evening schedules and dozens of degree programs. "Our world is being rapidly destabilized," Xavier University President Michael Graham said.

Some schools have taken drastic action. Miami University has cut its budget by $50 million during the last four years to offset spending in other areas, and committed to raising $50 million more for student scholarships.

Universities including Ohio State and Purdue have said they will freeze tuition. And the University of Dayton has pledged to match any tuition increase with new grants and scholarships.

But even with those measures, the system appears to be teetering on edge, as universities build up debt and continue to expand their campuses.

UC pays about $80 million in annual debt payments, the legacy of a billion-dollar building boom starting in the 1990s. UC isn't building buildings now but wants to spend $70 million to renovate Nippert Stadium.

Nearly every other college in the region is adding buildings – most financed by private donations – from a $4.2 million chapel at Thomas More College to a $50 million student center at Miami University.

The combination of unaffordable tuition, increased spending and billions of dollars of subsidized federal student loans has experts warning that universities can't survive without changing their business model.

Moody's Investors Service warned in January that universities "need to lower their cost structures to achieve long-term financial sustainability and examine the cost structure of their traditional business model."

Increasingly, the bond rating service wrote, students are choosing a college based only on price, putting "all but the most elite universities" on notice that they face a volatile financial future.

"Everybody knows there's a bubble," UC President Santa Ono said. "A lot of people are under considerable stress to come up with the funds to pay for higher education."

Nationally, tuition has more than doubled in the last 30 years. Americans have borrowed nearly $1 trillion to pay for college and continue to spend $400 billion a year.

Locally, tuition continues to increase every year, from $10,784 a year for Ohio residents at UC to $32,070 at private Xavier University.

Fueled by increasing tuition, universities walk the fine line every budget season, spending more on health care and student services while cutting enough spending in other areas to balance their budgets.

UC and Northern Kentucky University both have dumped millions into reserve accounts recently to offset cuts from Ohio and Kentucky taxpayer subsidies. "The reason tuition has been going up is not because expenses have been going wild," said Geoff Mearns, president of NKU, which has lost more than $3 million in state subsidies in five years. "It's because as a society we have been disinvesting in public higher education. I think that's a dangerous trend.

"I think what we'll see is continuous, dynamic change in response to these pressures," Mearns added. "I think the disruption will come over time. We need to change over time."

For many students, borrowing without knowing how they'll pay back the money is no longer a choice. It's something they must do to keep up.

"Education equals dollars," said Pam Cavalier of Evanston, a student at tiny Chatfield College's Over-the-Rhine campus. "It's not for saving the world. I didn't really think about the cost, because I knew everybody was leveraging those costs. That's the American way."

Pam Cavalier, a student at Chatfield College, says she knew full well that going into debt for college was something that everyone did. THE ENQUIRER/CARA OWSLEY

Could college tuition be the next crisis?

Some economists say the "college bubble" could be the next American economic crisis.

In the early 1990s, the Internet bubble propped up companies without traditional revenue or profits. Stock prices ballooned until investors bailed out in search of sustainable profits.

Throughout the 2000s, the housing bubble allowed some people to buy homes they couldn't afford. Home values inflated to the point that the market discovered that those mortgages couldn't support the securities that Wall Street packaged and sold to investors scouring for profits.

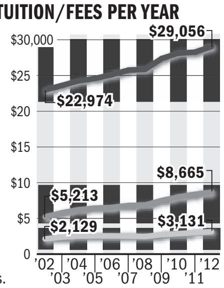
The current tuition increases share some signs of trouble: Skyrocketing prices are not cleanly linked to the value of the product, and there is a reliance on federal loans available to nearly anyone.

The difficulty in assigning a value to a college degree – why does Harvard cost nearly four times as much as UC? – provides an incentive to charge a higher price even if the product is not more valuable.

"Most market participants end up treating the price as a signal of the quality in both markets, meaning that a higher price will not necessarily scare away potential buyers, which certainly contributes to the formation of bubbles," wrote Andrew Gillen of the Center for College Affordability and Productivity in a 2008 study, "The Tuition Bubble: Lessons from the Housing Bubble."

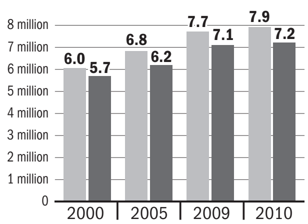
AVERAGE TUITION/FEES PER YEAR

Comparing **private four-year**, **public four-year** and **public two-year** institutions. Adjusted for inflation to 2012 dollars.



TOTAL FALL ENROLLMENT

Comparing **four-year institutions** and **two-year institutions** over the past decade.



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But some experts and economists point out differences. They say the housing bubble was based on greed while universities don't make a profit.

That discounts for-profits, which answer directly to shareholders aiming for quarterly Wall Street profits. That's why those universities spend hundreds of millions of dollars marketing to potential students, up to half as much as they spend on instruction. Those proprietary schools are in retreat in the face of increased regulation and criticism of the value they provide to students.

But for traditional non-profit colleges such as UC, Xavier or NKU, the profit motive is mainly designed to have enough cash to operate and a reserve to guard against future downturns. "In most institutions of higher education, prestige is the measure of success, not profit," Gillen wrote.

Warning signs of a bubble are everywhere for colleges

But the danger signs of an unsustainable trend are unmistakable:

» Colleges won't be able to make big tuition increases stick, Moody's said. College presidents agree that increases of more than 2 percent face the risk of being rejected by the market and students choosing other alternatives.

Ohio Gov. John Kasich is capping annual increases at 2 percent.

Moody's said one-third of universities expect tuition revenue to either decline or grow more slowly than inflation this year, up from 20 percent in 2008. That was before legislators and families started to push back against tuition increases of double the rate of inflation or more.

» Particularly in the Midwest, the supply of students is shrinking. The number of Ohio high school graduates will drop 9.3 percent from 2006 to 2022, shedding more than 12,000 graduates a year, according to the Western Interstate Commission for Higher Education, a membership and research group for U.S. colleges.

» Alternatives are springing up, particularly online and all at lower cost. Massive open online courses, known as MOOCs, are attracting 100,000 students or more and soon probably will translate to credit at UC, Xavier, NKU or other schools.

» Families are debating the value of the bachelor's degree. Surveys show about half of college graduates are working in a job that doesn't utilize their degree.

"Higher education is like the auto industry of the 1970s," said Tom Snyder, president of Ivy Tech Community College in Indiana. "It's lost track of the cost, it doesn't consider competition to be out there, and it's lost track of the needs of the consumer."

What could emerge from the current bubble is a world where the strongest and most prestigious universities, such as Harvard and Yale along with premier public universities including Michigan and North Carolina, will become stronger.

But schools that don't have a market niche will suffer, Ohio University's Vedder said. In Ohio, he could see public universities such as Kent and Akron being forced to merge.

That will lead to fewer choices for low-income students, he added. "I think college education is becoming much more stratified," he said. "These elite private schools are gaining on the good public universities."

The pin that pops the college bubble will be student debt, which will cause students and families to simply stop borrowing and forgo a particular college. "What we have is a failure of grants to keep pace with college costs, so college is less and less affordable," said Mark Katrowitz, publisher of FinAid.org. "The burden on the next generation is going to be that much greater. That's when you start to form a bubble."

Some predict the bubble won't burst at once but that universities will steadily see their financial strength erode, with high levels of student debt as a trigger. "Until consumers really demand something different, the way our debt policies work will allow it to continue to increase," said Rohit Chopra, student loan ombudsman at the federal Consumer Financial Protection Bureau. "It may not be a sudden calamity, but it could be a drag (on the economy)."

Pain in higher education would hurt local economy

If the "college bubble" pops, it also would hurt not only the employers of nearly 30,000 local workers, but also housing markets in surrounding neighborhoods and construction companies throughout the region.

Universities were among the few industries that continued to spend on construction, professional services and technology equipment during the recession.

And universities' roles in attracting talent and producing intellectual capital that creates new companies is the region's best source of future economic growth, said Dick Stevie, vice president of forecasting at local consulting firm Integral Analytics:

"It's innovation and new ideas that are the lifeblood of the economy here. It's part of our exporting-based economy. It's not exporting goods, it's exporting ideas. If you shrink that, you're going to shrink the economy."

Xavier's Graham said universities must find their own niche and exploit it. XU, he said, is considering a "pledge" to graduates that they would be employed in their desired occupation within six months or a year if they meet certain criteria.

"We have to be much more clear about the value here," Graham said. ■

HOW MUCH MONEY SHOULD YOU BORROW FOR COLLEGE?

The quick answer is only as much as you need. If you've already exhausted scholarships, grants and personal resources, then you may find you still need to borrow money to go to college. In fact, according to College Board, 64 percent of undergraduates end up borrowing at some point before graduation. If you need to borrow, here are some things to know in order to avoid borrowing more than you need.

Talk to someone you trust who is experienced in money matters. Perhaps that's a parent or grandparent. Or, it could be someone in your school's financial aid office. You'll learn tips and gain valuable real-life perspective.

Finance your education, not your lifestyle. Don't borrow more than you need. Student loans are intended to finance your school expenses, not your trip to Mexico for spring break. In fact, your school will usually be asked to certify that the loan will be used for school expenses. Remember, every dollar you don't borrow is a dollar – plus interest – that you don't have to pay back later.

Think about your life after college – you're going to have expenses. You might want to get a new car, take a vacation, or, eventually, buy a house. Smart planning now can help you afford those things later on.

Be responsible. Before agreeing to the terms of your student loan, find out what your expected monthly payments will be once your loan is in repayment. Keep in mind that you may need additional student loans to complete your degree – or even for graduate school. Be sure you're comfortable with your projected repayment amount.

Borrow less than what you expect to make your first year out of college, say many experts. While it's not guaranteed that you'll earn this amount, you can estimate what your potential first year's salary might be. The U.S. Department of Labor offers a helpful salary estimator.

Be aware of your future debt-to-income ratio. Generally, a financial adviser will encourage you to understand your "debt-to-income ratio" – the total of monthly payments on your debt load as a percentage of what you earn every month. After graduation, when you're looking to make a big purchase like a car or home, lenders will use this number to determine your ability to repay, given your current level of debt.

To figure out your debt-to-income ratio, try to estimate your future monthly *debt payments* – rent (or mortgage), car payment, student loans, credit cards, etc. – and your anticipated *monthly gross (meaning pre-tax) income*. Once you begin working, your **total** debt payments should be no more than 36% to 40% of your monthly gross income.

The concept of debt-to-income applies to student loans, too. You can calculate a student loan debt-to-income ratio by estimating your student loan payments as a percentage of your total income. After you've checked out the salary estimator above, Sallie Mae's Education Investment Planner can help you calculate what starting salary you'll need in order to afford your student loan payments. Then, based on the percentage of your income that will need to go toward your student loan payments (use the scale below for some benchmarks), you can build a responsible budget to help you live comfortably.

36% -40%

Once you begin working, your **total** debt payments should be no more than this amount of your monthly gross income.

» **10 percent or less: Manageable.** Your student loan payments are likely to be easily manageable on your starting salary.

For example, if you graduated with $25,000 in student loans (a typical amount for the 60-some percent of college grads who borrow), the monthly payments would be $288, so you would need a starting salary of approximately $35,000 to easily manage these payments.

» **11 percent to 19 percent: Caution.** Your student loan payments may be manageable as long as you don't have high credit card payments, car loans or housing costs. If your other expenses are higher, your loan payments may take up too much of your overall starting salary and you should explore other scenarios to pay for school so you can reduce the amount you need to borrow.

» **20 percent or more: Red flag.** You may have difficulty meeting your student loan obligations and other living expenses. You may want to reconsider how you will pay for school and explore lower-tuition schools. ■

Source: Sallie Mae's CollegeAnswer.com