

Challenges for Financing Public Higher Education

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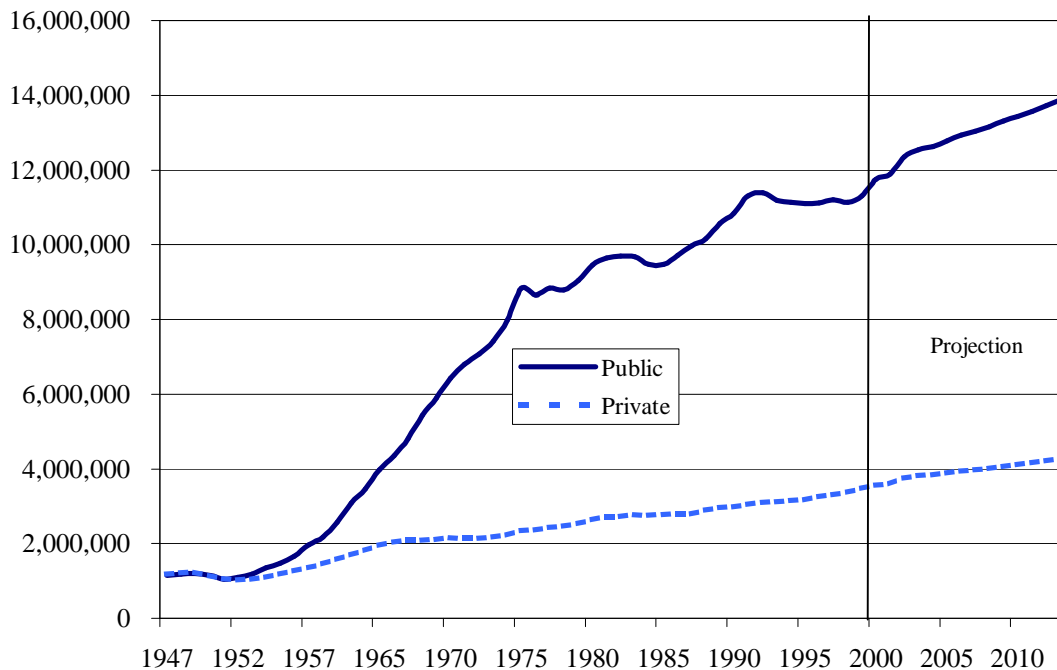
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Higher education, which includes all education past high school graduation, is essential in providing Americans with the necessary skills and abilities to compete in the increasingly competitive global marketplace. However, public higher education is currently facing many challenges. State funding for higher education has been declining both because of the recent state fiscal crisis and as a longer-term trend. The diminishing support from the state government has triggered significant increases in tuition and fees at public institutions. Meanwhile, many studies predict that the number of high school graduates will continue to increase. These problems bring into question the state governments' ability to finance public institutions as less expensive alternatives to private higher education.

Ever since early 1950s, public higher education has expanded much more rapidly than private higher education. Today, over three-quarters of all students in higher education institutions in the United States attend public institutions. According to the latest projections of National Center of Education Statistics (NCES), enrollment in public institutions will continue to grow in the next decade. (See Figure 1.)

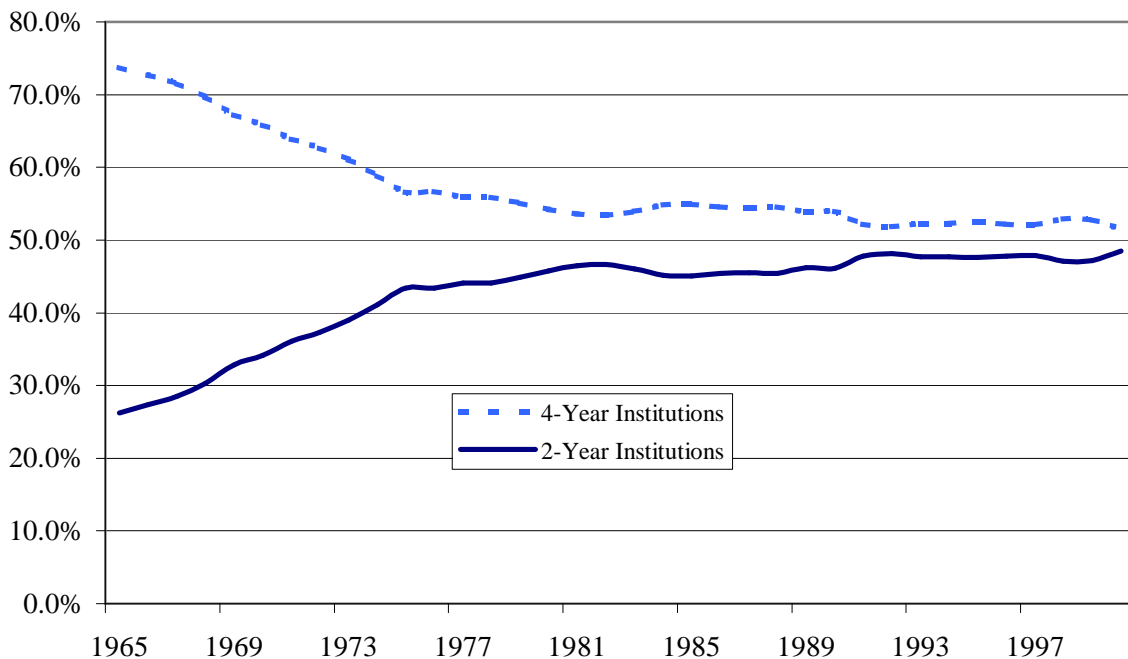
Figure 1.
Enrollment at Higher Education Institutions



Source: NCES *Digest of Education Statistics, 2002* and *Projections of Education Statistics to 2013*. Medium projections were used for all future values.

Two-year public higher education institutions, often called community colleges, have become especially important in providing Americans with the necessary skills to further their career objectives. As Federal Reserve Chairman Alan Greenspan recently pointed out, given the current state of the economy and concerns over lagging job creation, these institutions “have been in the forefront of teaching the types of skills that build on worker’s previous experiences to create new job skills.”¹ The share of students attending 2-year schools increased to over 45% of the total enrollment at public institutions by the beginning of the 1980s and has remained near that level ever since. (See Figure 2.)

Figure 2.
Enrollment Shares at Public Higher Education Institutions

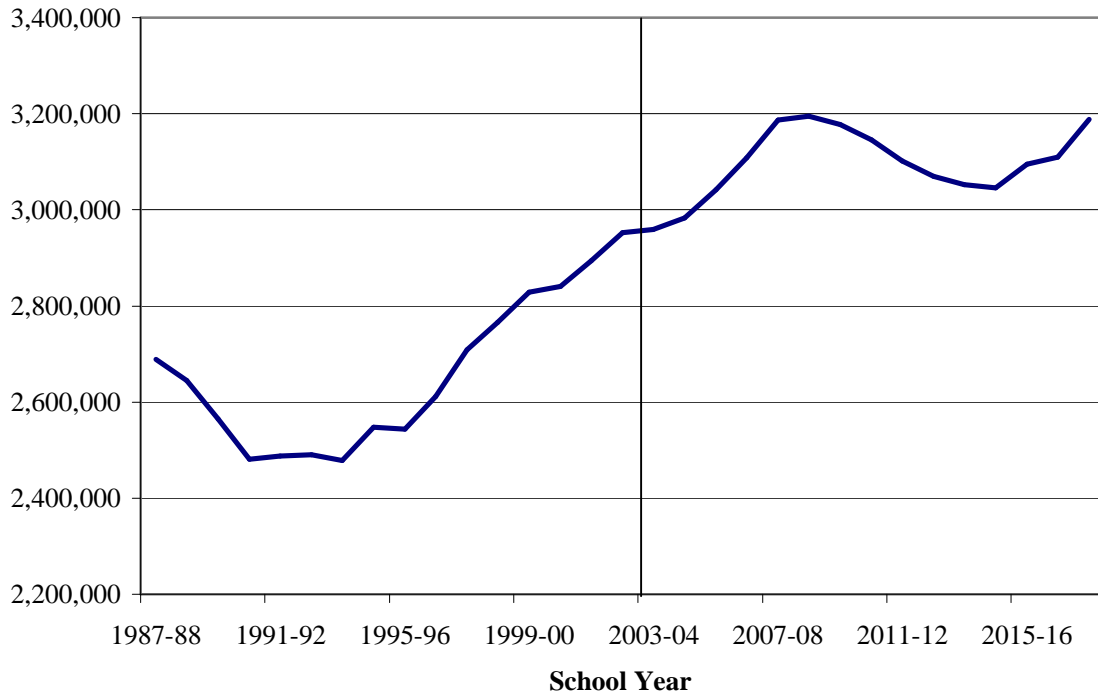


Source: NCES *Digest of Education Statistics*, 2002.

¹ “The Critical Role of Education in the Nation’s Economy.” Remarks by Chairman Alan Greenspan at the Greater Omaha Chamber of Commerce, 2004 Annual Meeting, Omaha, NE, February 20, 2004.

Another challenge is the movement of the “baby-boom echo” through the normal college years. The number of high school graduates is currently increasing rapidly and will continue to do so for several more years. (See Figure 3.) This will inevitably create a greater demand for higher education. This is particularly true in the states — generally in the South and West — with the most rapid population growth over the last few decades.

Figure 3.
High School Graduates



Source: Western Interstate Commission for Higher Education, *Knocking at the College Door* – 2003.

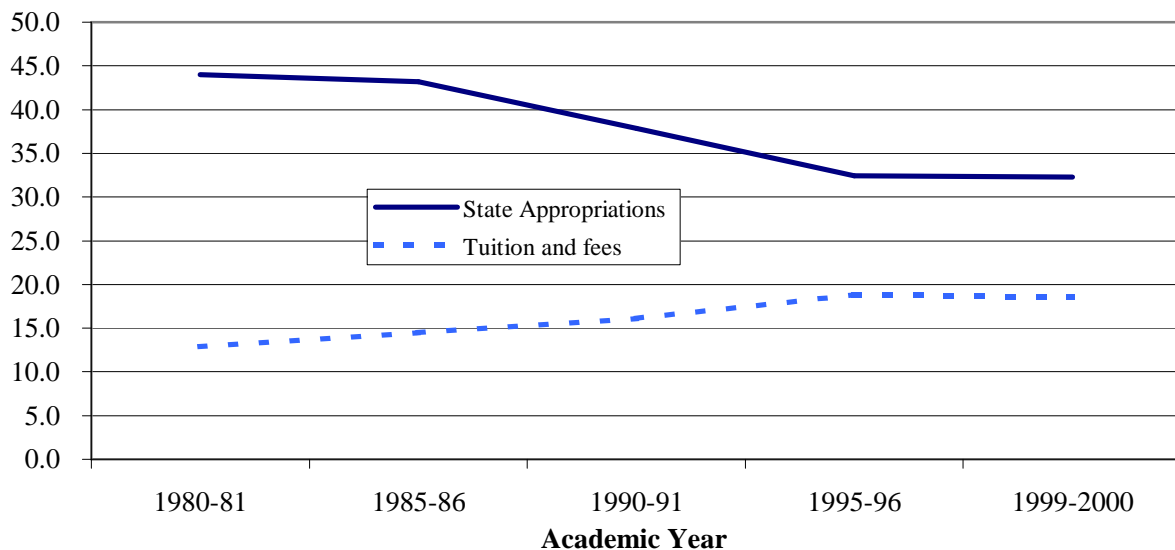
While the demand for public higher education is expected to continue to rise, the government's funding of higher education has been weakening. Public higher education is predominantly a state government function, rather than a federal or local function. As shown in Table 1, public higher education institutions received almost 36 percent of their income from state governments in the 1999-2000 academic year. However, as shown in Figure 4, the percentage of funds appropriated to public higher education has been declining while the percentage provided by tuition has been increasing over the last two decades.

Table 1.
Current-fund revenue of public degree-granting institutions, by source: 1999-2000

Source	Percentage
Tuition and fees	18.5
Federal government	10.8
State governments (appropriations and other)	35.8
Local governments	3.8
Private gifts, grants, and contracts	4.8
Endowment income	0.7
Sales and services	21.6
Other sources	3.9

Source: U.S. Department of Education, National Center for Education Statistics, Higher Education General Information Survey (HEGIS).

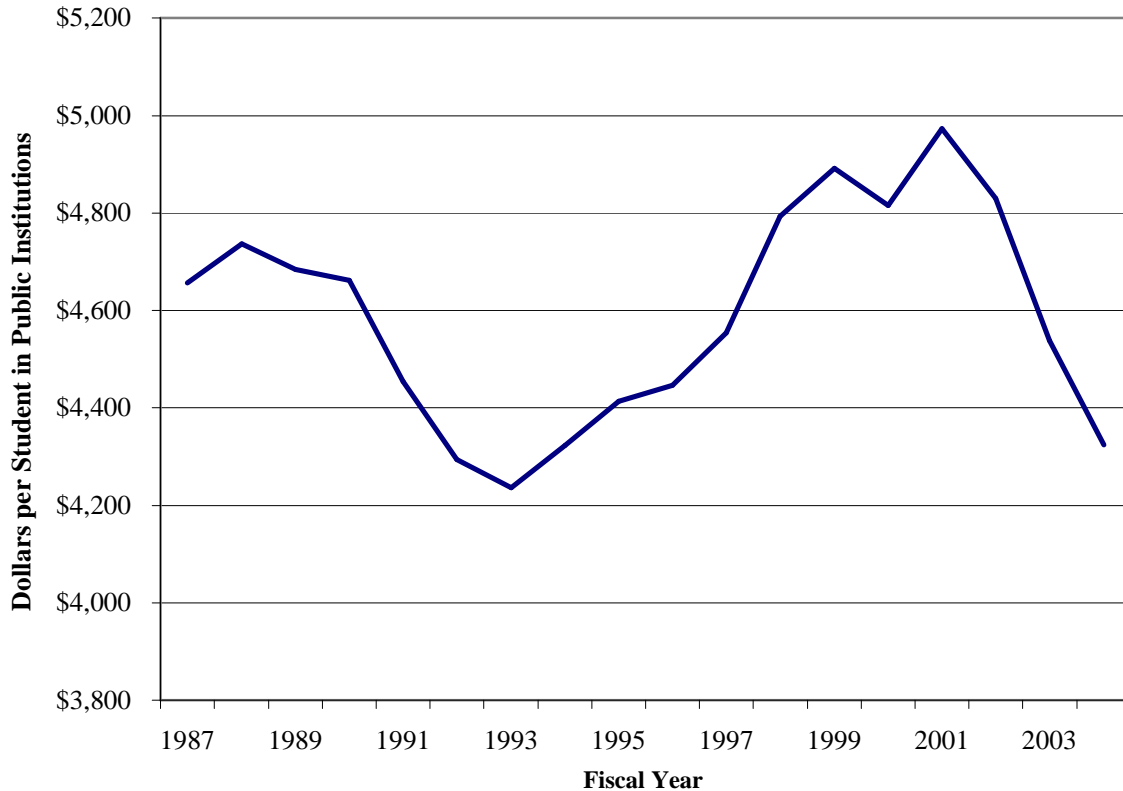
Figure 4.
Change in Percentage Share of Public Higher Education Funding 1980-2000



Source: U.S. Department of Education, National Center for Education Statistics, Higher Education General Information Survey (HEGIS).

Figure 4 ends in 2000, before the onset of the most recent recession. Since then, the trend has intensified. From fiscal year 2001 through fiscal year 2004, States have cut their appropriations for higher education by about \$650 per student in constant dollars. (See Figure 5.) This is a much more rapid and deep decline than was seen in the recession of the early 1990s.

Figure 5.
Total State Government Appropriations per Student
(Constant 2000 Dollars)



Sources: State government appropriations obtained from *Grapevine Database* at the Center for the Study of Education Policy, Illinois State University. Enrollment numbers from NCES' *Digest of Education Statistics: 2002* and *Projections of Education Statistics to 2013*. Inflation measured by the Bureau of Economic Analysis, State and Local Government Price Index for all years except 2004. For 2004, inflation measured by CPI forecast in Federal Reserve Bank of Philadelphia's *Survey of Professional Forecasters*.

Much of the recent declining trend in state appropriations for higher education is a result of the recession. However, higher education took a bigger hit from state spending cuts than any other major category of state programs. The ability of higher education institutions to raise tuition is one of the reasons for this. States could cut spending on higher education, raise tuition, and maintain services at about the same level – this sort of thing is not possible in many other program areas. The result has been that tuition has increased by an average of nearly \$800, or 22 percent, in just two years — from the 2001-2002 school year to the current 2003-2004 school year.

The cyclical trend may reverse itself as states emerge from the fiscal crisis caused by the 2001 recession, but the long term trend for state funding of higher education suggests that there is something else that is causing a decline in state support for public higher education. A paper by the Urban Institute suggests that much of this decline can be explained by the increasing demands of Medicaid on state budgets.² According to this analysis, states apparently began shifting resources from higher education to Medicaid during the 1990s. The way that federal aid works contributed to this: while states gain federal matching funds as they increase Medicaid spending, they may actually gain federal aid to lower-income students as they raise tuition. To the extent that the trend continues, the outlook for higher education is grim indeed, since every projection is for the cost of Medicaid to grow even more rapidly as baby boomers reach retirement age over the course of the next two decades.³

In conclusion, while higher education provides individuals with skills to participate in the increasingly competitive global economy, public higher education in the United States is facing a number of challenges that may weaken its ability to fulfill its functions. The most immediate challenge is from the large cuts that public higher education has taken as state have struggled to balance their budgets during their recent fiscal crisis. On top of this cyclical decline, there is evidence that states are reducing their support for public higher education over the long term, as other programs such as Medicaid require a larger share of public funds. Meanwhile, demand for higher education is likely to continue to increase, as more and more students graduate from high school each year. All in all these challenges are likely to create problems in the funding of public higher education for many years to come.

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² Kane, Orszag, and Gunter, "[State Fiscal Constraints and Higher Education Spending: The Role of Medicaid and Business Cycles](#)" Urban Institute, May 2003.

³ Ibid.