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Leveraging Crisis for Competitive Advantage

By John V. Lombardi May 8, 2009 6:32 am

The unusually large reductions in state appropriations to higher education in many states and the impact of the current record setting economic decline on other sources of university funding has pushed institutional responses into high visibility. We usually interpret America's never ending economic crisis in higher education as instances of unique phenomena, each one requiring new dramatic response. We react with surprise, alarm, and exceptional rhetoric to the cyclical downturns in public funding or private support. We dramatize the dire consequences that reduced funding will cause. We project an imminent decline in the international standing of American higher education as a result.

Yet, we weather these storms. Our traditional response is to lay off some people, cut back a few programs, delay some maintenance, and pull down our reserves. At the end of the cycle, we may be poorer, but we are not much different. Major research universities in particular are remarkably resilient enterprises. Constructed for the most part in cellular fashion, with each department, college, school, and unit operating almost independently within a national context rather than fully integrated into an institutional construct, the difficulties of one cell have attenuated impacts on others. Research universities generally protect core tenured faculty no matter what the fiscal circumstances, although they may reduce contingent faculty and dismiss staff in less critical areas. Universities have many open positions at any one time, and by delaying replacements, closing peripheral enterprises, and using reserves and other funds to buffer short-term losses, most institutions can find their way through a fiscal crisis without major structural changes to their operations, even when confronted with the dramatic reductions currently anticipated by many institutions.

Often, too, legislators and reform-minded politicians look to financial crises, especially ones as severe as this one, as devices for refashioning public colleges and universities in their own image. They want them smaller, less focused on research, more concerned with delivering job-related degrees to as many students as possible at unrealistically low costs. They imagine they can refashion the educational landscape using economic hardship as a primary tool. This effort generates much rhetoric from all affected parties, everyone seeking to highlight the benefit or damage such reforms might bring, and everyone being right to some degree.

This ritual cycle has its real victims in faculty careers delayed, employee jobs lost, and opportunities for students curtailed. Once the cycle of crises passes, however, the universities, like hardy boats in a storm-tossed sea, right themselves and continue sailing on in the same direction, restoring their damaged equipment as best they can while maintaining their course.

Dramatic realignments and restructuring of higher education only rarely result from the downturns of American economic life, but beneath this cycle of crisis, complaint, response, damage, and repair another less visible but nonetheless significant realignment takes place. The intense competition in American higher education, especially among the top 200 or so American public and private research universities, turns always on the fulcrum of money. Research university competition runs on human talent, whether students, faculty, or staff. The quality and productivity of people determines the winners in this competition. These quality people have the common characteristic of mobility: They can go wherever they believe their talent will find the most support and reward. The money determines which institutions can purchase the largest number of productive high talent people.

The economic cycles of American university life substantially affect the ability of institutions to sustain their competition for the best people: the more severe a financial crisis, the more significant the impact. The consequences of poor institutional response to a crisis tend to erode competitiveness over time rather than generate a dramatic crash. If a university focuses on its competitive context as it adapts to a financial crisis, it will make adjustments that enhance its ability to beat the competition when the crisis recedes. If the institution seeks to minimize internal conflict and maximize stability and continuity, it will almost surely weaken its competitive strength as it emerges from crisis mode.

University competitiveness is a function of how much money the university can spend on quality after it has paid for its sustaining operations. The critical issue in a crisis, especially a severe reduction in revenue, is preserving that margin for competition rather than spending the margin to sustain the status quo. Indeed, a truly competitive institution will reduce its expenses MORE than required; recognizing that as everyone recovers from the financial storm, the institution with money to spend on new people and their programs will have a relatively short period to outbid everyone else for talent, and at lower cost. Institutions that spent their margin sustaining what they had before, and often borrowing into the future to maintain the past, will find the improved economic benefits, when they come, already committed to the deferred costs of the crisis decisions made earlier. By the time they recover and begin to build a margin, they will find themselves behind in the competition for the best people.

This formula is simple and everyone should understand it, but acting on it is quite difficult. Universities are collaborative enterprises, they always seek to minimize conflict and maximize agreement, they have multiple constituencies that fight amongst themselves over declining resources, and they often have leadership concerned with maintaining the collegiality that builds career advancement. In public universities, governing and coordinating boards may be highly political and responsive to the short-term interests of the institution's many clients and supporters. Legislators may demand quick-fix solutions, and the public may find higher education's lament only semi persuasive. Private universities, already more coherently managed and with the ability to act in real time with a clear focus on institutional self interest, generally although not always respond better. In the constantly recurring cycle of financial crisis and university response, the benefit of private focused governance gives these universities an edge, especially during severe reductions in state revenue that limit the advantage of public university tax-based subsidies. Over time, and sequential budget crises, that edge helps explain the ability of private research universities to pull ahead of their public competitors in many areas.

Dramatic, revolutionary change does not readjust the competitive hierarchy of American research universities as much as the consistent pursuit of high quality, supported by a financial model that produces a consistent marginal surplus for investment in competitive people. That marginal surplus need not be large, but the university must deliver it consistently and invest it effectively. When that happens, it produces an institution whose competitive quality increases steadily and inexorably over time.

University competition is a game played on the leading edge of institutional behavior, not at the center. The optimal strategy is to move money from the less productive trailing edge to the more productive leading edge. Executed consistently over time, this strategy delivers an ever-increasing leading edge of highly competitive quality that pulls the center of the university's operations relentlessly forward towards higher standards of performance. The financial crisis cycle provides periodic opportunities to move more money from the trailing edge for investment in the leading edge. Those institutions that take advantage of these crises benefit greatly.