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SPECIAL COMMENT

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Rising Student Applications Complicate College Enrollment Projections and Budgeting

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Analyst Contacts:

NEW YORK +1.212.553.1653

Michael Osborn +1.212.553.7108
Assistant Vice President - Analyst
michael.osborn@moodys.com

Susan Fitzgerald +1.212.553.6832
Senior Vice President
susan.fitzgerald@moodys.com

Kendra Smith +1.212.553.4807
Managing Director - Public Finance
kendra.smith@moodys.com

Edie Behr +1.212.553.0566
Vice President - Senior Credit Officer/Manger
edith.behr@moodys.com

Karen Kedem +1.212.553.3614
Vice President - Senior Analyst/Manager
karen.kedem@moodys.com

Summary

US colleges and universities face increasing budgeting challenges due to the growing, but misleading, high volume of student applications. College planners and budget officials are receiving more applications, but not more students, as the number of applications per student is rising across the industry. This dynamic, which has been building for years, has reached a point where traditional models overestimate student demand and entering classes are yielding lower than expected numbers of students. Tuition-dependent colleges, especially, are vulnerable to budgeting and enrollment management challenges.

The new norms in enrollment management contribute to the following challenges:

» **Application growth leads to an artificial and inflated view of increased demand.** Between 2004 and 2013, applications increased nearly 70% for private colleges, compared to a 5% increase in the number of high school graduates over the same timeframe.

» **Disappearing yield contributes to greater enrollment uncertainty.** The percentage of admitted students who choose to enroll, known as the yield, is dropping. A growing number of colleges enroll less than 20% of their accepted students, making it increasingly challenging to predict and budget enrollment.

» **Savvier prospective students as well as economic and political conditions will keep tuition constrained despite increasing applications.** To enroll students, colleges are increasingly competing on price, limiting growth in tuition revenue and increasing discounting. In FY 2013, net tuition per student failed to grow by at least 2%, our proxy for inflation, at 35% of private universities and 26% of publics. Our tuition survey projections for FY 2014 highlight even greater price sensitivity.

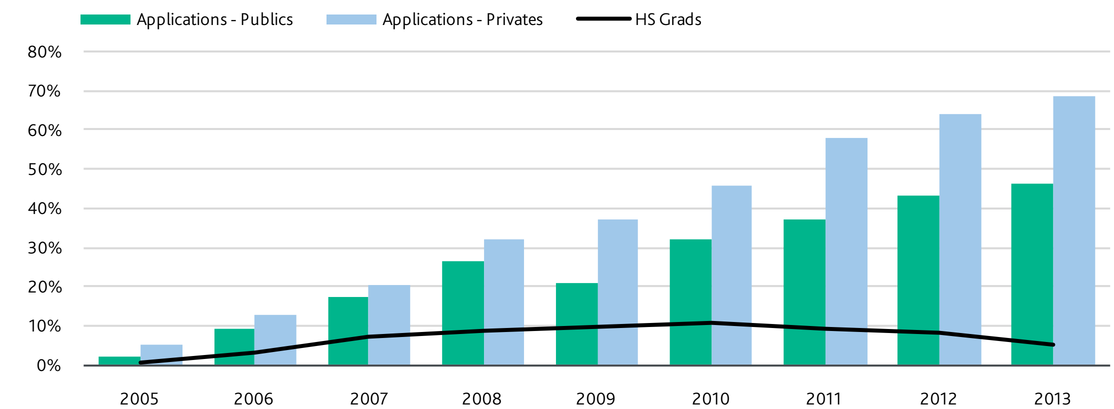
Application growth leads to an artificial and inflated view of increased demand

Application growth will continue to exceed growth in the numbers of domestic high school graduates as colleges broaden recruiting strategies and students apply to more colleges. Most colleges continue to expand applicant pools in hopes of optimizing the academic quality and diversity of their student body while growing top-line revenue. In fall 2013, the ten-year cumulative growth rate in applications at private universities approached 70% compared to only 5% for US high school graduates (see Exhibit 1). Technological advances will continue to facilitate further growth, lowering the costs of traditional recruiting in new markets and enabling colleges to maintain regular contact with prospective students.

EXHIBIT 1

New Applications Far Outpace New Students

Cumulative % Growth in Applications versus Cumulative % Growth in High School Graduates



Source: Moody's Investors Service; Western Interstate Commission for Higher Education, Knocking at the College Door: Projections of High School Graduates

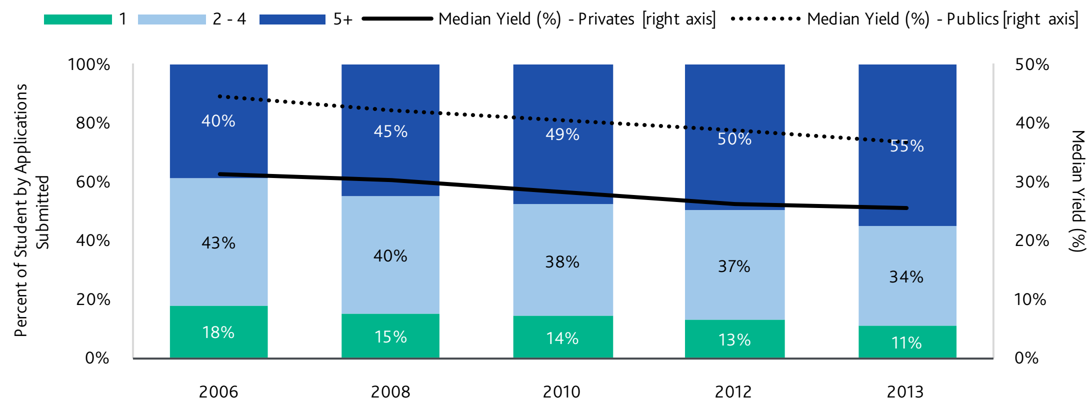
Students' quest for the best financial aid package and their concerns about being accepted to selective colleges also spur application growth. In 2013, 55% of students applied to five or more colleges (see Exhibit 2). As a result, nearly half of colleges and universities (60% of privates and 30% of publics) admitted less than 60% of applicants in Fall 2013. In 2004, only a third had such strong selectivity statistics. The trend of increased perceived selectivity is common to both publics and privates. However, with nearly half of all schools having a decline in their Fall 2013 entering class, it is clear that selectivity has become less useful as an indicator of true student demand.

Many schools have simplified the application process for students with the move to a common application, managed by a not-for-profit membership organization called the Common App (not rated). With the Common App's removal of the essay requirement effective with the 2015/2016 recruiting cycle, membership to the organization will likely increase and the number of aggregate applications will likely climb even further.

EXHIBIT 2

More than Half of Students Submit Five or More Applications

Number of Applications Per Student



Source: Higher Education Research Institute, UCLA, The American Freshman, National Norms; Moody's Investors Service

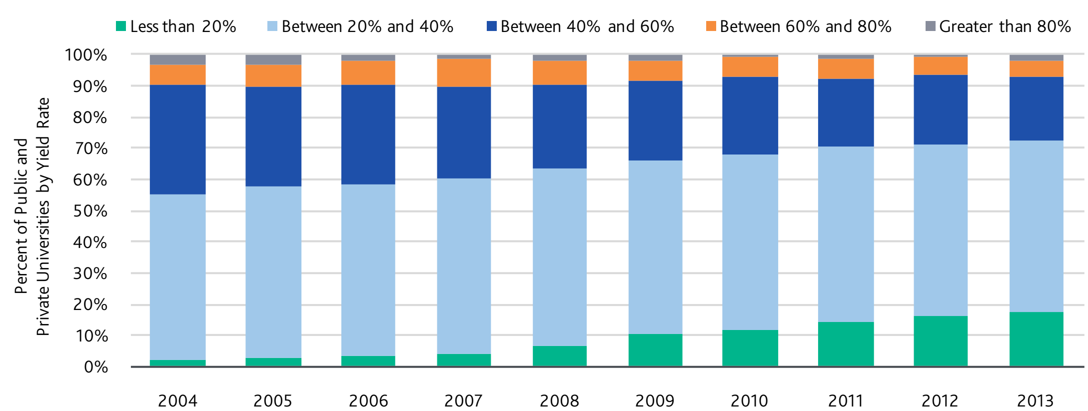
Disappearing yield demonstrates rising enrollment uncertainty

Colleges confront ever greater enrollment uncertainty as the yield rate on accepted students continues a steady downward march. Planners face growing challenges in predicting which students within the growing applicant pools are most likely to enroll. In Fall 2013, nearly 20% of colleges and universities had yield rates of under 20%. This compares to just 2% of institutions with similarly low yield rates a decade earlier (see Exhibit 3). The entering class declined by 5% or more at over 20% of institutions, public and private alike, in fall 2013. For both publics and privates experiencing this magnitude of decline, the median acceptance rate of applicants was in the mid-60 percentile range, with a median yield rate of 20% for privates and 35% for publics.

EXHIBIT 3

Ultra-low Yields below 20% are Spreading Across the Industry

Yield Rate on Accepted Students



Source: Moody's Investors Service

Application growth is not correlated with rising net tuition

While rising applications would traditionally correlate with increased demand, and therefore greater pricing power, this is not currently the case for many colleges and universities. Higher education institutions are pursuing sophisticated pricing strategies in an attempt to meet multiple competing goals, including achieving targeted enrollment, growth of total tuition revenue, and shaping of the class to meet diversity and other goals. As students become more savvy and competition more fierce, discount rates continue to climb. Twelve percent of private universities now have a tuition discount rate (i.e. financial aid or scholarship) of over 50% compared to 5% of private universities in 2004.

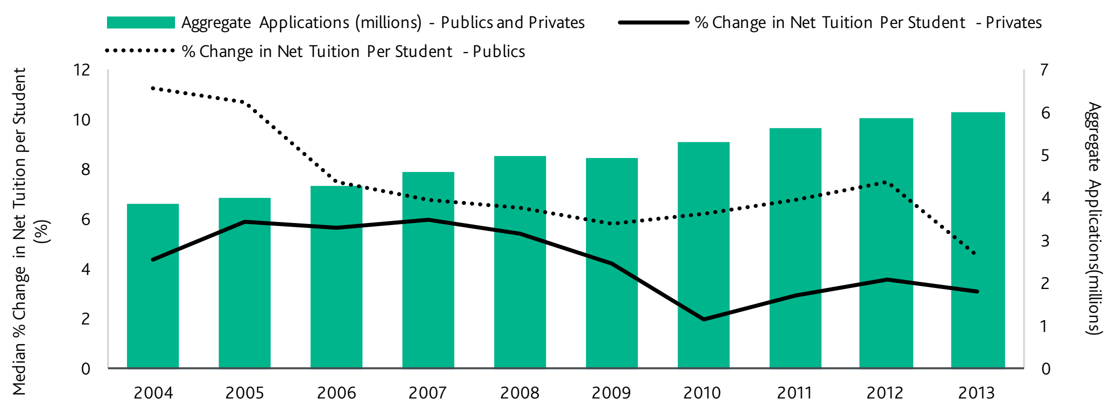
Public universities are increasingly employing similar strategies as the privates as they look to expand their geographic reach in response to demographic and economic pressures in their own states, as well as limitations on increasing in-state undergraduate tuition rates. According to Moody's, forty-four percent of regional public universities and 39% of flagship universities and systems now discount tuition by over a third.

The competitive student market, combined with political and regulatory initiatives attempting to improve college affordability, will keep growth in tuition revenue constrained. Sector wide operating pressure will grow as student charges are the largest revenue contributor for both the public and private university sectors. In FY 2013, the median net tuition revenue per student growth slowed to 3.1% and 4.7% at private and public institutions. Net tuition revenue garnered per student failed to grow at 2%, our proxy for inflation, at 26% of publics and 35% of privates in FY2013. Our FY 2014 tuition survey projected over 40% of publics and privates would fail to grow net tuition revenue by over 2%.

EXHIBIT 4

Net Tuition Per Student Slows Despite Increase in Applications

% Change in New Tuition Revenue Per Student



Source: Moody's Investors Service

Moody's Related Research

Industry Outlook:

- 2014 Outlook – US Higher Education, Not-for-Profits and Independent Schools, November 2013 (160659)
- Outlook Update: US Higher Education: Negative Outlook for US Higher Education Continues Even as Green Shoots of Stability Emerge, July 2014 (172857)

Median Reports:

- Stability of Fiscal 2013 US Private University Medians Masks Underlying Pressure, July 2014 (172855)
- Growing Pressure Evident in Fiscal 2013 Public University Medians, July 2014 (172867)

Special Comment:

- Weakened Tuition Revenue Plagues US Higher Education, November 2013 (160487)

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Author
Michael Osborn

Editor
Susan Fitzgerald

Associate Analyst
Matthew Kuchtyak

Senior Production Associate
Vinod Muniappan

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