

USC CENTER FOR HIGHER EDUCATION POLICY ANALYSIS

Higher Education and the Global Marketplace

*Entrepreneurial Activity in a
Dynamic Environment*



27th Annual Earl V. Pullias Lecture

In

Memoriam

The Pullias Lecture is dedicated to the memory of Earl V. Pullias. Through the lecture series and the publication of Pullias' publications, many people the world over have come to know his ideas.

"You can be no better teacher than you are a human being," he said. Those who knew him or knew of him remember the human being: an inspired teacher, a thoughtful, articulate scholar and a unique friend who continues to inspire.

**Higher Education and the
Global Marketplace:**

*Entrepreneurial Activity in
a Dynamic Environment*

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Introduction

Among the most dynamic influences affecting higher education is the increase in the for-profit postsecondary industry. In 2002, for-profit institutions constituted 12% of the four-year colleges and universities in the United States, continuing a rapid pace of growth that began in the late twentieth century (NCES, 2003). As the economy moves towards a more knowledge-based labor market, for-profit institutions will continue to play a significant role in providing individuals with the requisite knowledge and skill sets needed to compete in the job market. Declining state revenues for public higher education may suggest that an institution's status as either public or private is less relevant than how well the institution is meeting the current needs of society. In order to better understand these competing frameworks for higher education, the Center for Higher Education Policy Analysis hosted *Higher Education and the Global Marketplace: Entrepreneurial Activity in a Dynamic Environment* as part of the annual Pullias Lecture series.

Dr. Lloyd Armstrong, the former provost and senior vice president of academic affairs for the University of Southern California from 1993 to 2005, discusses the changing environment affecting higher education that brings the different market sectors of the research university and for-profit institutions together. He considers this interaction within the framework of innovation—when a new sector of industry, such as for-profit institutions, brings unique strengths to create a dynamic interface. The resulting goal for research universities is to sustain innovation that strengthens their existing services. Ultimately, both sides learn from the other to better serve their constituencies.

Mr. Douglas Becker provides a personal perspective on the mission, goals, and growth of the for-profit postsecondary industry. Mr. Becker, the chairman and CEO of Laureate Education, Inc., draws on his experience operating numerous for-profit universities in countries around the world. The goal for Laureate is to foster institutions that serve local needs and are situated within the local culture, but also expose students to the rapid globalization of the 21st century. He maintains that the research university and the for-profit institution share many goals: expanding access, graduating capable students, and providing a well-grounded education for the student's investment.

The rapid growth of for-profit institutions raises questions regarding the nature of higher education and its role in furthering economic, social, and intellectual developments. The purpose of the lectures are not to compare which system of higher education is more effective in furthering the public good and goals of society. Rather, they are intended to provoke dialogue and discussion about two inherently different educational approaches to achieving such goals. The rapidly changing landscape of higher education in the new century will influence public discourse regarding the role of the university within the larger context of society. For-profit colleges and universities, without doubt, will be included in such discussions.

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I. Introduction

THIS PULLIAS LECTURE provides an unusual opportunity for representatives of two different sectors of the non-profit and for-profit worlds of higher education to peer into the future of higher education together. For my part, I will talk about what I know best, the research university as it has evolved in the United States. Research universities and the for-profit academic sector have moved along until recently with little real interaction or interference. However, the environment for higher education is continually changing, and change is often the stimulus that brings different market sectors into direct contact.

In considering how these two market sectors might interact in the future, I find it useful to draw on the concepts of sector competition developed by Christensen in *The Innovator's Dilemma* (1997), and by Christensen and Raynor in *The Innovator's Solution* (2003) (for simplicity, these two books will be referred to below simply as "Christensen"). Each analyzes a situation in which there is a sector of an industry that is established, highly respected, and extremely successful; a newer sector also exists that is evolving into direct competition with existing institutions. At the outset, the newer sector appears to be producing an inferior product when measured against the quality criteria or value metrics of the established sector. However, under certain conditions, the newer sector evolves into a highly competitive position vis-à-vis the established sector, and in the process, changes the value metrics of the entire

sector to reflect its own special strengths rather than those of the older sector. The interaction of the extremely successful research university and the much newer for-profit higher education sector can be considered very naturally within this framework.

Christensen points out that the business model of any sector contains the seeds of its own destruction, fault lines that appear under certain conditions that enable a successful challenge from a competitor. I begin in Section II by describing several characteristics of the modern research university that help to highlight the differences with the for-profit sector. I also discuss one characteristic of the research university that provides a potential fault line. In Section III, I outline the environmental changes facing higher education. These changes will force evolution within the research universities—what Christensen calls *sustaining innovation*—and open up opportunities for other types of educational institutions to move into the space of the research university—what Christensen calls *disruptive innovation*. In Section IV, I share my personal view of the evolution that will take place in the research university in response to these pressures; and in Section V, I talk about the existing interface between the non-profit and for-profit sectors.

II. Present Status of the Research University in the United States

The American research university is arguably the most powerful force in higher education worldwide.

THE AMERICAN RESEARCH UNIVERSITY is arguably the most powerful force in higher education worldwide. Internationally, other institutions seek to emulate its successes in research, education, and economic development. The success of the research university is closely tied to its unique mission and organizational structure; these same attributes, however, create challenges to its continuing achievements.

The American research university “bundles” three missions: research, education, and abundant (and expensive) opportunities for social growth for its students. This bundling alone does not distinguish the research university from many excellent liberal arts colleges—but the magnitude of the entire operation and the intensive focus on research does. Within the educational component of the mission, the research university provides undergraduate programs, master’s degree programs, and doctoral programs in the traditional arts and sciences. Almost all also offer a variety of professional degrees (e.g., M.B.A., M.D., Ed.D., J.D.) as well as research-based Ph.D.’s in professional fields. There is extensive cost sharing and shifting among these components. This combination of mission, scope, and emphasis has proven to be quite attractive to parents and students, and over the years, an increasing fraction of “traditional” undergraduate students have chosen to do their studies within this segment of the higher education marketplace.

For the most part, these institutions do focus on “traditional” students—that is, undergraduates who enter college directly from high school, and graduate and professional students who attend essentially full-time. In general, the premier research universities are highly selective, with very high entrance standards for students at all levels. Although their students may be drawn from a large, often global, constituency, most research universities are geographically “local” in the sense that they are physically located in a single city or town. As in almost all of non-profit higher education, the students are expected to come to the institution, rather than the institution going to the students. Continuing education does not play a major role in the strategy or mission of most of these institutions, although it can be an explicit component of the mission for many state institutions. Business and engineering schools are the most likely components of the university to provide aggressive exceptions to this rule, and may have very extensive continuing education components (often called, in the former case, executive education).

Only a very small fraction of accredited institutions of higher learning are considered to be research universities. Of the roughly 3,600 accredited institutions, only about 200 would be considered to be research universities; the American Association of Universities (AAU), which has as its members the elite of this small set, has only 60 American member institutions (plus two more from Canada). Nevertheless, the impact of this relatively small set of institutions on

The interlocking missions of the research university provide enormous benefits, but also the potential for instability.

research and education in the United States is huge. They provide about 16% of the total research and development carried out in the United States (roughly \$44B in 2002), and most of the basic research (61% in 2002) (NSF, 2002). About 81% of annual federal university research funding goes only to the top 100 institutions in this set, with over 60% of the annual total federal university research funding going to the 60 American members of the AAU. In addition, since these research universities are the primary institutions that award the Ph.D. in the United States, most college and university faculty in this country have graduated from one or another of this small number of institutions. This movement of faculty from the research university to other elements of the higher education system brings a strong element of consistency of intellectual background, understanding of academic quality, and expectation of rewards to the entire system.

With their intertwining missions of research, education, and social development, American research universities have become very large organizations. Most have annual budgets well in excess of \$1B. They provide unequaled opportunities for learning and social growth for a certain type of student, and are the sources of some of the best research in the world.

The interlocking missions of the research university provide enormous benefits, but also provide the potential for instability. Over the past half century, the research component of the mission has increased enormously in magnitude and cost. Faculty who are very successful at research

are very expensive, and their central role in the educational programs of the research university increases the cost of the educational mission. Similarly, the laboratories in which so many of the students enjoy a research experience working under the direction of a faculty member are enormously expensive to build and maintain. Based in large part on what is now called co-curricular activities, the “social growth” mission increasingly demands expensive residence halls and varied dining opportunities, luxurious athletic facilities, an enormous range of student clubs and activities, and a large staff to support all of these activities.

However, the benefits of the differing elements of these missions are not uniformly received by all of the students of the university. For example, graduate and professional students generally are much less interested in the social growth element of the university mission than are the undergraduates. Professional students, although they may be delighted to have a class with a professor who has written a key text in their field, generally do not benefit directly from the research infrastructure, and relatively few undergraduates are directly exposed to the benefits of research. Thus, many of the students are overserved by the research university, that is, forced to pay for features that they do not fully utilize and consequently do not value highly. As pointed out by Christensen, such a situation leaves an organization open to attack by competitors who are better able to match their product and price to the actual needs of some portion of the organization’s customers. While the reputational strength of the

research universities provides considerable protection from this type of instability, it would be unwise to assume the protection is absolute or unlikely to change with time.

III. The Evolving Environment for the Research University in the United States

ALTHOUGH THERE ARE MANY ASPECTS of the educational environment that are changing, five stand out as potentially requiring both sustained innovation on the part of the research university, and an opportunity for the for-profit sector to advance through disruptive innovation.

Increasing “winner-take-all” competition among research universities.

A “WINNER-TAKE-ALL” SITUATION (Frank & Cook, 1995) is one in which the winner at one stage of competition is better prepared to win at the subsequent stage as compared to other competitors. Higher education has transformed into a “winner-take-all” situation over the past decades, and might now be considered to be advancing into the mid-stages of the process.

It is very difficult to compare the actual value of an education gained at one university or college with that which could be gained at another. There simply are too many variables involved, compounded with the fact that different people seek different things from their time at a university. Consequently, much of the reputation of a research university is based primarily on more eas-

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ily measured metrics—the quality of its students and the quality of its faculty. Quality of students is typically reflected by measures such as SATs, GPAs, demonstrable artistic talent, and the like. Quality of the faculty typically is measured through such outputs as grants, books, and awards. Use of these metrics is, of course, not unreasonable. The quality of much of the learning and social growth at a college or university is directly tied to the quality of a student’s peers; on average, students who enter college with the best preparation are also most prepared for the next stage of education or work when they graduate. It is the faculty who are active in advancing the frontiers of knowledge that subsequently have the most opportunity and potential to involve students in their work and to share their discoveries with students, thus fulfilling a key premise of the research university.

Reputation is, of course, a critical factor as universities vie for the best students and faculty, and for government grants and private donor dollars. Reputation is also a critical determinant in defining the desirability of a university’s graduates to employers. Thus, it is in the university’s interest to increase its reputation compared to the reputations of its competitors, for this will enable it to obtain additional resources that will lead to increased reputation. It is just this sort of non-linear feedback that leads to a “winner-take-all” situation (Frank & Cook, 1995).

In order to attract the most talented students, universities and colleges are increasingly required to differentially subsidize their educa-

tion through merit scholarship aid. Although this has only recently become a major issue at the undergraduate level, it has been commonplace for a long time at the Ph.D. level. The Ph.D. is, in many ways, the “highest” and most prestigious degree awarded by a university. It is enormously expensive to provide because it requires an extended one-to-one relationship between a faculty member and a student, as well as very expensive facilities. In addition, the better Ph.D. students will only be attracted by an aid package that will include not only a full tuition fellowship, but also a “competitive” multi-year stipend that may or may not require some teaching service. As competition for better Ph.D. students increases, the enticement that was once aimed at a relatively small number of the best students has been extended to almost all Ph.D. students in the major universities. Thus, the hunt for the best students requires universities to give away their product—in the case of the Ph.D., their most expensive product—in order to be competitive.

There has been a parallel growth in the resources dedicated to the socialization component of the mission. Dormitories have become residence halls, gyms have become recreation centers, cafeterias have become food courts, and student services budgets have ballooned. Parents and prospective students have increasingly paid attention to this component of the mission as choices are being made, and invidious comparisons between competing universities are to be heard in any conversation involving prospective students and their parents.

Attracting and retaining the best faculty is also a difficult and expensive proposition on many fronts. Almost by definition, there are never enough “best” faculty to go around. This leads to bidding wars between institutions that not only drive up the top end of the salary range considerably, but also lead to such expensive practices as reduced teaching loads and highly flexible leave arrangements. The best facilities are required to attract these faculty, which significantly increases the university’s construction budgets. Finally, research of these faculty is seldom self-sustaining, and requires a broad variety of university subsidies in order to thrive.

All of the elements described above are quite expensive, such that the universities with the best cash flows are best able to compete effectively for the best students and faculty. Having the best students and faculty then increases the excellence of the university, which generally leads to improved cash flow, and so on. This cycle, which Winston (2001) has described as a “positional arms race,” begins to move the best students and faculty into a smaller and smaller number of institutions. Because of the peculiar nature of the higher education enterprise, this cycle will not lead to a literal “winner-take-all” situation. No university would aspire to be the size required to house all of the “best” students and faculty, nor is the public likely to accept a single definition of what the “best” university is. However, this cycle does drive up costs significantly for most colleges and universities, and is slowly creating perceived quality gaps between groups of institutions.

Changing societal expectations.

JAMES DUDERSTADT (2002) has eloquently defined a major change in the way society and government views its institutions:

It is important to remember that most of our institutions were the result of public policy and public investment through actions of governments at the national and regional level. Yet today, in the United States and many other nations, public leaders are increasingly discarding public policy in favor of market forces to determine priorities for social investment.

Ample evidence would indicate that, in this matter, public leaders are in tune with the general population. This view is consistent with Bobbitt's thesis (2002) that a major evolution in governance is taking place worldwide, with the nation state being replaced with the market state. As a consequence of this change, institutions of higher education find both increased societal skepticism that their existence is a good thing in principle (an acknowledged public good) and corresponding growing demands that they demonstrate a response to the needs of society. Funding agencies now commonly require that even the most basic of projects contain some component that responds to a societal need, e.g., better K-12 education or increased economic development. Federal funding patterns progressively emphasize biomedical research that can lead, sooner or later, to better health, or to engineering research that can stimulate economic growth. More and more,

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research universities are valued by their communities because of the positive impact they can have on regional economic development.

The effects of market forces are not trivial to predict. For example, will the market view education as a public good or a private benefit? Will it view education as an entitlement, or an investment in the future?¹ Each possible combination of these attributes would favor a different type of educational experience. Thus, predicting the evolutionary effects on the university that Duderstadt has described is not straightforward, but it seems almost certain that there will be major effects in all components of the mission.

Increasing globalization.

THE LAST CENTURIES have shown a steady and dramatic growth in globalization, although political events have often affected its pace and form. Rapidly developing communications capabilities that do not recognize national borders have provided a major stimulus to this trend. Economies, cultures, politics, and science are increasingly global, rather than national in character. Similarly, issues and concerns of significance to societies—e.g. the environment, disease and health, the economy, and government—are linked intrinsically to global drivers. Thus, universities seeking to respond to societal demands for relevance will find themselves invariably pushed into the international arena. Education itself must reflect these changes, and students must become comfortable and skilled in working across national boundaries if they are to excel in this new environment.

¹ I thank Phillip Bobbitt (private communication) for suggesting these possible market responses.

Many research universities provide significant continuing education to corporations, usually through their business or engineering schools. As corporations become even more global, the universities also must become global in their outreach if they are to be able to continue to serve their corporate customers effectively wherever their needs may occur.

At the same time, one sees that the American dominance in higher education is being challenged on all sides. Research universities are gaining rapidly in quality in many areas of the world where only a few years ago there were no real research universities. In many cases, these institutions are being built on the American model, with leadership trained at American universities. Many excellent international students who, in earlier times, would have had no choice but to come to the United States for a high quality university education are finding that a viable substitute now exists at home. In other areas of the world where excellent research universities have long existed, such as Europe, England, Australia, and Canada, market forces are pushing universities to become aggressively global in their search for students. The resultant competition for international students is made increasingly severe by security measures implemented in America after 9/11 that directly target international students. These measures have had the effect of greatly reducing the desirability of an American education for many international students.

Faculty will need to focus more on guiding students to an understanding of the meaning and uses of information.

Changing access to information.

THE CONTINUING ENORMOUS ADVANCES in information technology (IT) are revolutionizing how we think about information, and consequently redefining authority relationships within the university. In many ways, the university and its faculty used to “own” information, and students had to come to the university to learn the desired information. The Internet has now made information enormously accessible, which will certainly lead to significant changes in the way students learn. Faculty increasingly will need to step out of the role of authoritarian provider of information, and focus more on guiding students to an understanding of the meaning and uses of information that can be obtained from other sources. Higher level cognitive skills such as “critical thinking” will become a major objective of education, rather than a byproduct. This will require many important changes in the academy. Teaching faculty will have to understand the large volume of research on methods for teaching such skills. Many current faculty expectations will be challenged as this research is heeded. For example, faculty now have enormous leeway in preparing their courses, and need pay only minor attention to the details of other courses in the curriculum. However, much of the research speaks to the importance of threading key concepts through multiple courses, requiring a degree of coordination in course development which many would likely claim violates “academic freedom.”

As information becomes more accessible at a location chosen by the student, rather than

that defined by the presence of the university, other pressure for other changes will occur. For example, universities will be challenged to find ways in which to carry out their educational mission at sites chosen by students, rather than at the site where the university has chosen to locate. Similarly, twenty-four/seven access to information will raise issues around the old concepts of four year bachelor's degrees, nine-month school years, 9:00am-4:00pm school days, and one hour classes.

Changing demographics and the growth of the knowledge economy.

THE NUMBER OF HIGH SCHOOL graduates has grown significantly over the recent past, leading to increasing enrollment pressures at the better colleges and universities. However, this number will peak in about 2008, and then drop over the next roughly 8 years by about 8%, finally returning to the 2008 peak by about 2018. In the United States, this rise will primarily reflect increases in populations that have not traditionally been strongly attracted to research universities, such as underrepresented minorities, especially those who are first generation college attendees. In order to maintain their present undergraduate student populations, research universities either will have to capture an even larger market share among traditional students, or will have to become more attractive to underrepresented minority students. Ibarra (2001) suggests that universities might be more attractive to underrepresented minorities if the universities were to better integrate academic programs by addressing real societal issues.

At the same time, the growth of the knowledge economy will emphasize the critical importance of lifelong learning. Mature, employed workers will increasingly demand advanced education and credentialing so that they can better thrive in the marketplace. However, for these workers, the opportunity costs of returning to the university campus for any extended period of time will be much too high for that to be a practical option. Universities that seek to participate in this growing market will have to develop new approaches that enable high quality education under conditions of time and place that are quite different from those generally encountered today.

IV. A Personal View of the Future for Research Universities

SIMPLY IDENTIFYING SOME of the instabilities that might affect research universities does not indicate how society will value universities in the future, or how the best universities will evolve. In this section, I describe my own personal view of the way in which external societal expectations and market forces will combine to shape the future of the non-profit research university in the United States.

First, the increasingly market driven society will have evolving expectations for research universities. An increasingly important metric of excellence will be the ability of a university to make important contributions to significant

An important metric of excellence will be the ability of the university to make contributions to social problems.

social problems, rather than to create knowledge that is valued primarily by peers at other universities. Although all research universities will be affected to some degree by these evolving expectations, some set of major research universities will accept societal impact as a key component of their missions. Creation of new knowledge will remain the core mission of the research university, but faculty in these universities of societal impact will increasingly seek to place and direct their research within a broader societal context. Large, complex issues such as health promotion and care, urban sustainability, effective governance, education, immigration, and job creation will come to play a more prominent role in the portfolio of these universities' research and teaching. The Cartesian dichotomy between basic and applied research (Toulman, 1992) will largely fade as researchers come to grapple with the larger unknowns of these complex issues. Collaboration of these research universities with other types of institutions within society (e.g. NGOs, government agencies, and museums) will increase as the universities seek to use their newly created fundamental knowledge to impact major problems.

Second, the changing IT environment and increasing market competition will push research universities to focus more on the learning needs of the students rather than on traditional institutional structures and constraints. New learning technologies will enable the educational experience to be more closely aligned with the learning styles of individual students. Greatly increased flexibility in terms of timing and location of the learning

experience will be introduced. The important socialization aspect of the undergraduate experience will continue to impose many traditional limitations on time and location, but a large fraction of these limitations will disappear at the graduate and professional level. Many research universities will build a significant capability in continuing professional education, and success in this area will be dependent on creating a learning-centered environment.

Third, the global reach and presence of many research universities will increase greatly and change qualitatively. As noted above, issues of significance to society are increasingly global in nature. Those universities that choose to emphasize issues of societal impact will need to create an international presence to facilitate the research of their students and faculty, and to enable access to policy makers worldwide whose cooperation will be necessary to move research into practice. University competition for the best students will increasingly be global, and a learner-centered educational emphasis will require universities to provide opportunities for those excellent students at locations that are appropriate to the needs of the students. These two strands of research and education are mutually reinforcing because educating the best students from a region provides increased access to present and future policymakers of the region.

V. The For-Profit/Non-Profit Interface in Higher Education

The for-profit educational corporations are targeting a student population that would not be appropriate for a research university.

WITHIN THE RESEARCH UNIVERSITIES, the for-profit higher education world is most commonly either ignored or dismissed as low quality. It generally is felt that the for-profit educational corporations are targeting a student population that would not be appropriate for, or attracted by, a research university. Further, it is claimed that these corporations are providing students with an education that is inferior in one or more dimensions to that of a university.

There is, indeed, some truth to these allegations, at least as viewed from the merit system of the research university. For example, none of the for-profit institutions seeks to integrate experiences in cutting edge research into the curriculum, and none seeks to provide the kind of social infrastructure that is such an integral part of the university experience. In addition, from the perspective of the research university, the sacrosanct teaching role of the university professor has been deconstructed and devalued in the many segments of the for-profit sector. For example, while the university professor designs her class, teaches it, and then tests the students for comprehension, in the for-profit sector, these three tasks are often performed by three separate individuals or teams.

However, viewed from another perspective, one can see that the approach of the for-profit institutions fits very well the description of a disruptive technology (Christensen, 1997; Christensen & Raynor, 2003). First, they have

succeeded in reaching a portion of the public that otherwise would not have participated in higher education because of background deficiencies, time, limitations, or cost constraints. Christensen would call this successfully competing against non-consumption. The product that is offered generally has a direct payoff because it focuses primarily on developing skills that can bring job advancement, rather than on the more abstract, high-level skills that are the focus of most of the non-profit educational sector.

In their approach, the for-profits have succeeded in at least partially unbundling the high cost, three-layered mission of the research university. Education has been separated from the other components, thus significantly reducing its cost. The resulting educational product is clearly different from that offered by the research university, less rich in several dimensions. However, because they have been successful in finding an underserved consumer audience for their product, the for-profits have the opportunity to improve their product over time. Over the longer term, this improving product may give these institutions the potential to make disruptive inroads into some portion of the existing students of the research university who feel over served by the bundled offerings (and the corresponding high price) of the research university.

As described by Christensen, much of the radical innovation in a field comes from institutions that are moving into the field with a simpler, “inferior” product. The successful new products do not measure up to the dominant ones

in some dimensions, but respond effectively to a set of unmet or over-served needs through the introduction of a new approach. This new approach brings with it some benefit or values that are not emphasized in the original product, and as the new product increases in quality over time, the associated new value increases in visibility and importance among the entire customer base.

Examples of the kind of innovation described by Christensen can be seen easily in the for-profit educational system. The University of Phoenix, for example, has succeeded in part because of its focus on service and convenience for its students. Inquiry by prospective students, registration, and advising are all handled in ways that emphasize customer satisfaction and convenience rather than institutional bureaucracy. Phoenix offers multiple sites, carefully chosen to provide maximum accessibility, and coordinates course schedules to facilitate attendance by working adults. And, of course, Phoenix has been a very successful early advocate of on-line education, which further increases the convenience factor for its students. In many aspects, Phoenix now provides attention to student service and convenience that could become a new standard.

Laureate Education, on the other hand, is innovating in a very different direction. Laureate is in the process of creating the first truly global university. This new entity is dedicated, as stated on its website, to bringing “to its universities and students a global perspective blended with a local point of view, creating a truly multi-cultural, career-oriented educational experience.” The

accompanying lecture by the CEO of Laureate, Doug Becker, describes this enormously interesting venture in more detail.

Reputation, as mentioned above, is critical at the research university end of the higher education chain. Since reputations take enormous resources and generations to build, the very importance of reputation provides a substantial shield against encroachment by other types of institutions into the territory occupied by the research university. Thus, direct competition with the for-profits is unlikely to cause significant damage to the research university in the near future. However, the research universities ignore the innovative developments of these competitors at considerable risk. Our customers, though they may choose to stay with us for reputational and other reasons, may nevertheless have evolving expectations that are set by what they see in the for-profit world—that is, they may expect the best of both worlds, and we will need to try to provide it.

Even if we are afforded some protection by reputational shields, the for-profit sector is changing the environment in which we operate. Their presence has forced changes in a number of areas in order to remove barriers to their activities. For example, accreditation has been revised in significant ways in order to encompass for-profit institutions, and further changes are likely in the future. Many in the non-profit sector believe these changes have weakened accreditation and lessened its value; the for-profit sector typically responds that the changes simply have removed

The future will offer possibilities for some mutually beneficial collaborations between non-profit and for-profit educational institutions.

artificial protectionist barriers to their activities. The unarguable reality, however, is that accreditation is changing under pressure from the for-profit education industry, and will continue to change. Another area in which the environment has changed is federal financial aid to students. Due to both rule changes and participation rates, an increasing fraction of federal student financial aid is now going to students at for-profit educational institutions. The for-profits have also been successful in focusing the attention of many in the federal government on the question of transferability of credits between institutions, with the goal of enforcing some type of universal transferability between accredited institutions.

This interface, then, is a dynamic one. The rules and laws governing higher education are changing in ways that increase the potential for competition between and among the parties on the two sides of the interface. Considerable educational innovation is occurring on both sides of the interface. On the non-profit side, most of the innovation is what Christensen calls sustaining –innovations that make the existing product better. On the for-profit side, much of the innovation is disruptive, that is, providing entirely new products or a new value twist to an existing product. Both sides can benefit by learning from the other as we all seek to better serve our many constituencies. It is likely that the future will bring increasing competition between the sectors, with potential for acrimonious confrontations. It is equally likely, however, that the future will offer possibilities for some very exciting and mutually

beneficial collaboration between non-profit and for-profit educational institutions that are willing to move beyond the traditional views of each other.

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FOUNDED IN 1999, Laureate Education, formerly Sylvan International Universities, emerged early in the 21st century as a recognized leader in international higher education. Laureate currently owns and manages 18 different higher education institutions in 11 countries. These institutions serve 130,000 students on 42 campuses and another 20,000 students who are obtaining their full degrees via internet-based distance education. While a few of these institutions are specialized schools, most are structured as comprehensive universities and enjoy the highest form of recognition, licensure, and accreditation in their home countries. We are focused on building a uniquely international network of universities—each firmly rooted in its own local culture, but able to provide our students and faculties with unusual and extensive exposure to the rest of the world.

I. Laureate Education: An International Focus

UNIVERSIDAD DEL VALLE DE MEXICO (UVM) is an excellent example of the Laureate approach. Founded in 1960, UVM is well known and respected as a mid-tier institution aimed at expanding access to postsecondary education for middle-class Mexican students. Today, UVM has 19 campuses serving nearly 50,000 students at the undergraduate and graduate levels. It was recently listed as the 10th best university in Mexico in a *Reader's Digest* survey that is the country's equivalent to the *US News and World Report* annual rank-

ing in the United States. But more notable is that the nine institutions that were ranked higher than UVM either represent the elite “free” (or very low tuition) public universities that reject most applicants or the elite private institutions that charge a fee double or triple the UVM annual tuition of about \$3,500. Through UVM, Laureate is delivering recognized quality education while adhering to a mission of access and affordability.

Universidad Nacional Andres Bello (UNAB) in Chile is another outstanding Laureate institution. Like UVM in Mexico, UNAB is a comprehensive institution, offering degrees in law and medicine as well as business, engineering, education, and many other programs. Its medical school is a source of particular pride for UNAB, and the university is engaged in a number of prestigious research initiatives. Its three campuses currently serve approximately 20,000 students. In recent surveys, students and parents indicated that UNAB was their top choice of university, particularly for those unable to obtain admission to the famously selective Universidad de Chile and Universidad Catolica.

As may be evident by these examples, Laureate is assembling a postsecondary network with a focus on the Spanish-speaking world. In addition to universities in Mexico and Chile, we operate outstanding universities in Ecuador, Peru, Costa Rica, and Panama, and also in Spain, where our entire project began with the 1999 acquisition of the Universidad Europea de Madrid. We have since moved beyond the Spanish world with universities in France, Switzerland, China, and the

We have focused on providing an optimal mix of quality and affordability, with preparation for a successful career as our central objective.

United States. In entering most of these countries, we were driven to address the international lack of access to university education. Unlike the United States, which offers the greatest number of seats and the widest array of choices in higher education, in most parts of the world university education is only available to an elite few. Governments typically provide a free university education only to a small number of students with the highest scores, who, ironically, are often those who went to the most elite and expensive private high schools.

From the beginning, we have focused on providing an optimal mix of quality and affordability, with preparation for a successful career for each student as our central objective. In general, we have been embraced by the government in the host countries, who want to expand university access, but do not have the financial resources to do so. In fact, governments typically put their funds and energies into improving elementary and secondary education, which exacerbates the problem of supply/demand and creates an imbalance in higher education by increasing the number of high school graduates, more and more of whom seek higher education as they anticipate careers in the new economy.

Generally speaking, private universities are still a relatively new phenomenon in many countries. In many cases, public universities resist the expansion of the private postsecondary sector and often seem jealous of their success. Laureate's structure as a for-profit corporation is far less notable or controversial than the mere fact

of its private status. Because they are free (or extremely inexpensive) and often turn away many applicants, public universities become out of touch with students and employers. Students are viewed as “lucky to get in.” Our approach of treating students as clients is considered alien. Likewise, employers are expected to adapt to the workforce produced by the universities, rather than setting the standards for what university graduates can do. Saddled with external political interference and a challenging internal governance structure, the public universities are extremely slow to adapt to change. In fact, in many countries, the institution’s faculty elect those who administer the public universities. While a powerful voice for faculty can be desirable, some checks and balances are needed to ensure that other important constituents—parents, students, employers, and regulators—are heard as well.

The next stage of development for Laureate may in fact be the most exciting. Having established a successful local presence in many countries, we are now weaving the network that connects our universities. We started with simple student exchanges between countries. We were met with strong student interest, but limited participation due to cost. Shared curriculum and faculty expertise is the next major frontier. We intend to leverage the strengths of our centers of excellence in various content areas. Examples of centers of excellence would be our world famous Les Roches Hotel Management School and the Glion Institute of Higher Education in

Switzerland, which enjoy regional accreditation in the United States, as well as recognition by the local government and the prestigious Swiss Hotel Association. The École Supérieure du Commerce Extérieur (ECSE) and École Centrale D'Electronique (ECE), our schools in Paris, have also earned strong reputations in international business and engineering, respectively.

We chose to complement public schools rather than trying to supplant them.

II. Laureate Education: A Historical Perspective

LAUREATE'S ENTRY INTO the university arena and our mindset itself comes from our own background in private sector education activities. While now an independent, publicly traded company, Laureate was created in 1999 as the higher education division of Sylvan Learning Systems, known for its ubiquitous Sylvan tutoring centers throughout North America. These centers, which now number over 1,000, provide individualized assessment and instruction to children in elementary and secondary schools. In my 12-year tenure as the Chief Executive Officer of Sylvan, I had the opportunity to think very hard about the appropriate role of the private sector in a field dominated by the public sector.

We chose to complement public schools rather than trying to supplant them. Along the way, we learned a great deal about marketing to consumers and achieving customer satisfaction through delivering measurable results. Parents bringing their children to Sylvan expected results,

usually in the form of higher grades in school and better self-esteem for their children. Parents had no obligation to remain with us. We earned their loyalty and the right to a repeat visit with every single hour of instruction. When I joined the company, I recall that the average parent brought their child in for 28 sessions of one hour in length. Today the figure is around 84 sessions. Imagine, parents paying for something that most of them get “for free” from local public schools—instruction for their children. But the form of instruction, the selection and training of the teachers, the content, and the system produced results, and the parents were willing to pay for those results.

By understanding and meeting our customers’ needs and delivering results, we grew tutoring enrollment at Sylvan Learning Centers to over 200,000 students. Along the way, we ended up hiring over 25,000 teachers. When we came to the conclusion that training and developing qualified teachers was going to be critical to maintaining our growth, the groundwork was laid for our entry into higher education. Our 1997 acquisition of Canter and Associates was the first step. Canter was a teacher training company, but their fastest growing offering was a master’s degree for teachers. Over time, we came to realize through Canter that we could build an attractive business by focusing on postsecondary education. We grew the Canter distance-learning program into the largest master’s degree program in the United States—today 13,000 teachers are enrolled. Teachers are a perfect audience for this type of offering. They are looking for practical, relevant

content in their graduate programs that they can apply immediately in the classroom. They want to hear from recognized experts and practitioners, and they are anxious to complete their degree because they are assured of a wage increase once they do so.

Teacher education became the foundation for our Laureate Online division, which today offers graduate degrees through our own Walden University and National Technological University, both regionally accredited by the Commission on Higher Education of the North Central Association of Schools and Colleges. In addition to our master's degree programs in business, engineering, information technology, public health, public administration, and many other fields, we also offer Ph.D. programs in many of these same areas and currently have over 4,000 doctoral students.

By 2003, postsecondary education had become two-thirds of our company revenues, and we decided to spin off our elementary and secondary education businesses, including the Sylvan Learning Center network, into a completely separate company that is now publicly traded as Educate, Inc. We then renamed our existing public company Laureate Education, focusing this firm on postsecondary education. The combined revenue of Laureate and Educate now approaches \$1 billion annually.

III. For-Profit versus Non-Profit

Because we tend to focus on preparing students for the job world, practical experience is essential.

IN THE PROCESS OF building Sylvan, we had to bridge the divide between the non-profit and the for-profit worlds. Initially, we faced the stereotypes that are typical to this debate. For-profit companies can be painted as mercantile and greedy—but efficient. The non-profits are often viewed as inefficient, yet compassionate and ethical. In fact, we all know examples of organizations on both sides of the divide that for better or worse defy these stereotypes. With the launch of Sylvan we set out to prove that we could match the values of the non-profit world with the accountability of the for-profit world. Could we embrace and exemplify commitment to community service while still operating as an effective business? Over time, we proved that we could. And in the process, we learned that the line between for-profit and non-profit can become very slender indeed.

Perhaps the best example of this thin line is seen in the clinical activities of our universities. Because we tend to focus on preparing students for the job world, practical experience is essential. In the case of many of our programs, such as law, medicine, physical therapy, and dentistry, we operate clinics that provide free or subsidized service to the community, while giving our faculty and advanced students the clinical experience they need. I recently toured a clinic specializing in support for autistic children at UVM in Mexico, one of very few such clinics in that country. There was nothing “for-profit” about the type of service we were providing to the families and the commu-

nity, or about the compassion and dedication of the faculty and staff involved.

We have not taken dividends out of any of our universities around the world. They are free to build their excess revenues and to re-invest those funds in facilities or programs that benefit our students and grow our business. Our universities do have to make a compelling case to us that value will be created from such re-investment. If we are re-investing all of the profits generated, how is this any different from a non-profit? The only difference in economic terms is that a for-profit business is taxable and the non-profit enjoys the substantial economic advantage of its tax exemption, a privilege it should be required to justify by the benefit that it offers society. In the United States there is currently a debate raging over the many instances of non-profit hospitals refusing emergency service to uninsured patients. Regulators are proposing that such hospitals must provide pro bono service or risk the loss of their tax exemption. A thin line, indeed.

But there are important and real differences between the two worlds, beyond taxation or values. Some societal needs, for example, can really only be served by the non-profit or public sector, and basic research is a good example. We are very careful to focus on areas that correspond with our corporate structure and business orientation. Research at our universities is fairly limited and the degrees that we offer tend to be based on the fairly immediate employment needs of a community.

If a student cannot see a return on investment on the tuition cost of their education, then we are not likely to offer the program. That does not mean that such a program is without merit. Rather it may be in an area that should be served by the public sector, which has a funding stream for that purpose. But these types of programs are becoming rare. Governments, especially in the United States, are increasingly favoring “user fees” as a funding stream, reserving general taxation to cover services for which no user could or would ever pay. This trend is seen quite clearly in public universities that gain an increasing portion of their revenues from tuition and user fees while support from the state is dwindling. The concept of user fees tends to align the interests of public, non-profit, and for-profit providers, requiring attention to the interest and needs of the user to attract and retain customers.

This concept of being customer-centered is not unique to instruction and student services. Every cost area must have a revenue offset, even—or perhaps especially—research. A research university such as USC is very “customer responsive” in choosing grant topics and approaches that match both the interests and parameters of the funding agencies. This is clearly the case for research, but is also relevant in university efforts to garner donations from wealthy alumni, for whom elaborate proposals are prepared based on research regarding the giving history and preferences of the donor.

In our case, we do not receive government grants or donations to any material extent, so we

Our total focus is on the needs of our students and on the requirements of the workplace that will employ them.

have just one revenue area to offset costs—tuition. Hence our total focus is on the needs of our students and on the requirements of the workplace that will employ them. Of course, many elements of the cost structure at USC (or any other public or private university in the United States) are also predicated upon generating tuition revenues, and the student recruitment process—with its wonderful euphemism of “enrollment management”—is clearly intended to secure and grow that revenue stream.

So if American universities are becoming more customer-focused, where are the meaningful differences between for-profit and non-profit institutions? I believe that the answer lies in accountability and compensation practices and important differences in governance that give the for-profit institutions a tremendous advantage. Managers in the corporate world are expected to measure performance and to raise it to meet objectives. Those who succeed will enjoy increased compensation. Those who do not show performance in achieving these metrics may eventually lose their jobs.

In our company, we have a “data driven culture.” We want to measure everything: student satisfaction, graduation rates, employment statistics, and student loan default rates. We measure our market share of matriculants from each area high school that feeds each of our university campuses. Our passion for measuring and improving has resulted in good results. At Walden University, as an example, we have brought our annual attrition down to approximately 10% while

reducing default rates on student loans to a remarkable 1.9%. All of this would already sound impressive, but it is even more so when you consider that we increased Walden's student enrollment from 1,100 to 11,000 in the same four-year period of time. These numbers are not just about "money." Lower attrition and student loan defaults are linked to quality. And we measure many other important aspects of the university—both reality and perception.

How many public or non-profit universities truly understand their profitability by degree program? This is a bedrock principal for us. We are not unwilling to lose money on a program, but it is unacceptable for us not to know about it. If there is a strategic or community service reason to lose money on a program, and we are prepared for it, then it is a conscious decision. But the non-profit world often has a harder time evaluating their business on this basis, given the intertwined and fixed costs involved. As an example, I recently read an article about the severe nursing shortage in my own home state of Maryland. It is estimated that we will have a shortage of more than 11,000 nurses in the state within a few years. Several of the top local universities have indicated that they would be unable to take on more nursing students without more state support. I believe that tuition from incremental students would cover the incremental costs to expand the program. But the universities just don't know.

Without good data, you cannot hold people accountable for results. But once you can, we have found that there must be consequences for

meeting or missing objectives. This is one area where the private sector excels. Because we know how much value is being generated by a particular activity, we can determine how to share that value in the form of variable compensation such as bonuses. This allows us to attract top talent, and to pay for performance. Team members in different areas are measured against different objectives such as growing enrollment, managing expenses, bringing construction projects in on time and on budget, reducing attrition, and securing jobs or internships for students.

But equally important to compensation for achieving results is the ability to replace people who are not performing. This does not have to be a draconian process. We can be patient and compassionate. We can coach employees to higher performance. We can put them into different roles that better match their skills and interests. In fact, given how hard it is to find great people, we cannot afford to discard people for the wrong reasons or without every opportunity to improve. Creating a warm environment with high morale is essential to achieving success. But if we have tried all reasonable remedies to no avail, we have to make a change.

This is where the public or non-profit university may be at a real disadvantage. It is very difficult to replace poor performers in most universities. While this may have started as appropriate protection to ensure the academic freedom of faculty, it has clearly leached into the entire enterprise. If your best performers are not compensated more generously than mediocre performers,

and you are unable to replace poor performers, it will be very difficult to succeed in an increasingly competitive world.

If a traditional university wanted to adopt a results-oriented culture, they would encounter the most difficult obstacle—governance. University governance was designed to ensure stability and balance. But this protection against bad decisions is equally resilient against good ones. In the for-profit world, decisions can be made much more rapidly. Entire organizations can be transformed to match changes, real and perceived, in the outside world. If the CEO misreads the environment or embraces a bad strategy, it can result in serious harm to an organization. But if she or he makes good decisions, the entire institution can respond to environmental changes and the needs of constituents in a way that traditional universities could never match. In our case, we strive for appropriate checks and balances to mitigate the risk of whipsawing the organization with impetuous decision-making. Each of our universities has a Board of Directors or an Advisory Board consisting of leaders in government, education, business, and culture in their country. And within each university, the views of academic leadership are solicited and accorded the deepest respect. The parent company itself, Laureate Education, has a distinguished board that cautiously evaluates the most important decisions. But when we decide to move on an issue or a new idea, we can do so faster and more decisively than any traditional university.

Ethics do play an important role in our

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decision-making, as would be the case in many traditional universities. We take our role in society most seriously. We view our mission of expanding access to quality university education as immensely important. What has been fantastic in my view, and perhaps surprising to the public, is how little compromise is required between business and social objectives. We understand that the reputation of the university has a direct impact on our enrollment and our length of stay. So it is easy to make decisions and investments that uphold the reputation of the university. We understand that the quality of our academic leadership and faculty is directly linked to our reputation and business success, so we take care to provide them with an attractive work environment, compelling compensation, and an important voice in the affairs of the university.

IV. The Future of For-Profit and Non-Profit Education

I HAVE TRIED TO FRAME the discussion by illustrating the similarities and differences between non-profit or public universities and our own for-profit approach. My objective has been to brush away the stereotypes to understand the true differences, which tend to emanate more from differences in customer type and expectations than from differences in values or morals. If for-profit universities can embrace quality, exhibit a commitment to society, and reinvest their profits into the institution and the community, then the

“moral edge” can be taken off of the debate and we can move to a more fact-based discussion.

The fact-based discussion allows us to weigh the advantages of each model and to try to predict how these models will fare in the future. On the one hand, we have for-profit institutions that are responsive to the needs of students and the workplace, driven by outcomes, and responsive to data. They are financially efficient and make decisions more rapidly than their traditional counterparts. They do not have the prestige to attract the most elite students and the very best faculty. They are not funded or structured to perform extensive research functions. They are, in short, ideally suited to their role as teaching institutions with a career-oriented focus.

On the other hand, we have public and non-profit institutions that run the gamut from community colleges to top research universities such as USC. And it is in that breadth that I think we can begin to see some signs of the future. Teaching institutions that try to meet the needs of the workplace are going to find themselves at a real disadvantage to the for-profit sector. The only exception will be for those students who lack money or access to funding—but in the United States, the Pell Grants and Title IV loan programs (and the declining state subsidies) currently serve to level that playing field. Outside of the United States, and in the absence of these financing mechanisms, the opportunities for the for-profit world are limited to those students who can afford to pay. Yet a responsive provider can design a service that many customers can afford. Our

tuition in some of our Latin American institutions can be as low as \$1200 per year.

In the United States, the institutions whose revenue model is based on student tuition, and yet which do not operate at an elite level, are the ones at risk. They will need to adopt the outcome-driven approach and the streamlined decision-making of the private sector. There are a number of examples of schools that already do this very well. Johnson and Wales—based in Providence, Rhode Island, but with five campuses across the nation—is a leader in culinary and hospitality education with over 15,000 students. It has the distinction of having once been a for-profit institution that later converted to non-profit status, the reverse of what I think we will see with certain universities in the future. It exhibits all of the efficiency and customer responsiveness of the private sector.

University of Maryland, University College is another excellent example. Started as the continuing studies “night school” of University of Maryland, it has become a regional powerhouse, serving the working professionals of Maryland. But it has gone beyond its home state to a true worldwide presence through extensive military contracts and a powerful online presence. University of Maryland, University College receives virtually no state subsidies or charitable gifts, and through tuition income alone is able to cover its costs and generate excess revenues to reinvest in the expansion of the institution. Other notable examples include National University of San Diego and Nova Southeastern

University.

These market responsive, fiscally efficient non-profits and their for-profit brethren will dominate the mid-market teaching institutions, especially in the area of working adult education. And the elite traditional universities, be they research institutions or the finest liberal arts schools, will continue to maintain their unique niche based on prestige, quality, and funding streams from research and philanthropy which cannot be matched by the for-profit institutions.

For our own part, at Laureate, we will not be that active in the fray in the United States. Our main focus remains the rest of the world, where this debate is truly—and the pun is intended—academic. In the many countries where they simply do not have the capacity to meet the needs of students and the workplace, our business structure is of little consequence. If we expand access, graduate capable entrants to the workforce, and deliver a return on the tuition investment of our students and their families, we will succeed in every way that matters.

APPENDIX

*About
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Authors

LLOYD ARMSTRONG, JR.

University Professor Lloyd Armstrong, Jr. served as provost and senior vice president for academic affairs at the University of Southern California from 1993 to 2005. He is credited with overseeing some of the most significant academic advances in the university's history.

Prior to coming to USC, Armstrong was on the faculty of the Johns Hopkins University. He arrived as a postdoctoral fellow in the physics department at Johns Hopkins in 1969 and rose through the faculty ranks, attaining the rank of professor of physics in 1975. He served as chair of the department from 1984-87, and as dean of the school of arts and sciences from 1987 to 1993. He spent two years as a Senior Physicist at the Westinghouse Research Center in Pittsburgh before going to Johns Hopkins.

Armstrong serves on the board of directors of the California Council of Science and Technology, and the Pacific Council on International Policy, and is a member of the Council on Foreign Relations. He is a fellow of the American Physical Society and has served on a variety of panels and committees for the National Academy of Sciences/National Research Council including chair of the committee on atomic and molecular sciences.

Armstrong received a B.S. in physics from MIT in 1962, and a Ph.D. in physics from the University of California at Berkeley in 1966. Following his Ph.D., he was a post-doctoral fellow at the Lawrence Berkeley Laboratory (1966-67).

DOUGLAS BECKER

Douglas Becker has led Laureate Education, Inc. (formerly known as Sylvan Learning Systems, Inc.) since 1991. As chairman and chief executive officer, positions he has held since 2000, Mr. Becker has overseen the transformation of the organization from a domestic tutoring company into a strong global leader in higher education. It was in recognition of its new focus on higher education that the company changed its name to Laureate Education, Inc. in 2004. As the only company operating large scale universities in multiple countries, Laureate is now recognized as one of the world's most promising international companies. Previously, he served as co-CEO of the company since 1995 and as its president since 1991.

*Previous
Pullias
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2003 Vincent Tinto, Ph.D.
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2003 Walter Allen, Ph.D.
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President Emeritus
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2001 Karen Symms Gallagher, Ph.D.
Emery Stoops & Joyce King-Stoops Dean
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2000 Arthur Levine, Ph.D.
President
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1999 Charles B. Reed, Ph.D.
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**1979 Norman Topping, M.D.,
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About
Chepa

The Center for Higher Education Policy Analysis (CHEPA) brings a multidisciplinary perspective to complex social, political, and economic issues in higher education. Located within the Rossier School of Education at the University of Southern California, the Center's director is William G. Tierney. Conducting theoretically informed research with real-world applicability, the Center has a broad focus on three areas of higher education—improving urban postsecondary education, strengthening school-university partnerships, and understanding international education, with a particular focus on the Pacific Rim.

The goal of the Center is to provide analysis of significant issues to support efforts to improve postsecondary education. Such issues intersect many boundaries. The Center is currently engaged in research projects regarding effective postsecondary governance, emerging organizational forms such as for-profit institutions, financial aid and access for students of color, successful college outreach programs, the educational trajectories of community college students, and the retention of doctoral students of color.

Over the last decade we have received funding from the Ford Foundation, the Pew Charitable Trusts, Atlantic Philanthropies, the James Irvine Foundation, the U.S. Department of Education, the William and Flora Hewlett Foundation, the J. Paul Getty Trust, Lumina Foundation for Education, and the Haynes Foundation.



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