

COME OUT STRONG

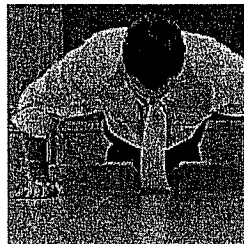
- E-MAIL
- PRINT
- FAVORITES
- SHARE

Has the recession worn you down? See how institutions are using a through-cycle strategy to anticipate recovery and prepare to emerge in even better shape than before.



By Margo Vanover Porter

"Most of us working in higher education today have not seen anything like the current recession," says Morgan R. Olsen, executive vice president, treasurer, and chief financial officer, Arizona State University (ASU). "The depth of the economic downturn is so significant that it requires us all to do things we've not been asked to do previously and think about problem solving in a different way. Like a number of other institutions," explains Olsen, "ASU has experienced major state appropriation reductions." In fact, he says, "they've exceeded 21 percent in a little over a year."



So what's a business officer to do?

Faced with dramatic losses in revenues and searching for answers, Olsen feels that the concept of a "through-cycle" mentality helps place emphasis on not only today and tomorrow but where the institution's leadership team wants the institution to be five years down the road.

"When you have such significant budget reductions that are mandated in a very short time frame—which was certainly the case for us and a lot of our colleagues across the country—you need to have a multipart strategy," Olsen explains. He and others in ASU's top leadership knew that they had to cut \$90 million out of their state appropriation by the end of the fiscal year that ended June 30. "In the short term," Olsen explains, "we had to find those savings wherever we could. But, ultimately, some of the things we're required to do are not sustainable or not optimal. So, we have a short-term strategy to deal with immediate imperatives; and longer term, we need to think about through-cycle management. That means asking: 'Where do we want to end up? How do we want the institution to look after we internalize these longer-term adjustments?'"

This longer-term perspective, notes Olsen, means ensuring that key investments continue to be made in people and facilities that will enable the university to thrive in a new, more austere environment. ASU continues to build such investments into its financial plans, taking advantage of the opportunities that the changing environment offers. This includes recruiting new, high-profile faculty and investing in critical research infrastructure that will allow continued double-digit growth in ASU's research

WAITING FOR THE NEW NORMAL

Once the recession ends—whenever that is—what will the new normal look like?

"It will vary by type of institution," predicts Paul Jansen, director emeritus, McKinsey & Company. "The new normal for the top-tier, well-endowed institutions will look a lot like the old normal. They have more than enough students trying to get in the door, and they have significant financial resources."

Dean Currie, vice president for business and finance, California Institute of Technology, Pasadena, points out that even though they are often lumped into one broad category, institutions vary distinctly by type. For example, a public state university is facing a different set of economic circumstances right now than a research institution. "We are in a fabulous environment for research universities," he says. "The

volume.

Paul Jansen, director emeritus, McKinsey & Company, first raised the idea of applying the concept of a through-cycle mind-set to higher education after reviewing McKinsey research on how companies fared during the 2000 recession.

"Leaders going into the recession did not always emerge as leaders coming out of the recession," says Jansen, who retired as a partner of McKinsey in June. "New institutions took their places. One hallmark of those that became leaders or stayed leaders was that they viewed recessions as opportunities to strengthen their own operations, improve their profitability by cutting costs, and capture near-term revenue opportunities."

Jansen also notes that those who finished on top also seemed to invest at differentially higher levels than their competition in research and development, in acquiring new talent, and in making acquisitions. "We characterize that," says Jansen, "as a through-cycle mind-set—managing through the cycle, anticipating a recovery, and making investments to position the institution to be very successful when the recession is eventually over."

RETAIN CRITICAL CAPITAL PROJECTS

Although originating in the business world almost a decade ago, the concept of through-cycle management applies to current strategies being adopted by colleges and universities. For example, Stanford University continues to invest in critical capital projects that position it for future growth, while curtailing other expenses.

"We've left behind a long period when revenues grew significantly faster than inflation, enabling the university to fund numerous new initiatives without cutting anything," says Randy Livingston, vice president for business affairs and chief financial officer, Stanford University, Stanford, California. "We believe revenue in the next decade is unlikely to grow faster than inflation. This means that to continue to fund new things, we have to find savings."

As a result, Stanford has laid off more than 400 staff and suspended approximately \$1 billion of capital projects. "At the same time, we are continuing with approximately \$2 billion of capital projects that we believe are essential to our future competitiveness and success," Livingston says. These include:

- o Lorry I. Lokey Stem Cell Research Building, a \$200 million structure that will be one of the largest stem cell research buildings in the world when completed early next year.
- o Center for Nanoscale Science and Technology, which will house faculty from multiple schools and disciplines focused on nanotechnology and reinforce the institution's emphasis on multidisciplinary research.
- o Knight Management Center, a new \$374 million campus for the Stanford Graduate School of Business to support a recently redesigned, flexible curriculum.

Livingston adds that Stanford is also building 39 new faculty homes to help address a chronic recruiting challenge.

RECESSION AS OPPORTUNITY

budget for the National Science Foundation, which is normally around \$5 billion, has an additional \$3 billion to give away in the next year and a half. However, we need to look across a favorable environment to one that will be much less favorable. When the bill comes due and the deficit has to be reckoned with, we need to make sure we're not putting back in place a high-cost structure."

Morgan R. Olsen, executive vice president, treasurer, and chief financial officer, Arizona State University, believes that the new normal for a few elite universities may indeed look like business as usual ... but other institutions will face serious change. "We've been an industry that has changed relatively slowly," he says. "I don't know that we'll continue to have that luxury. We will have to respond to questions about value-added, cost-effectiveness, and productivity. Given the demographics and economics of the country, we are likely to see institutions providing a range of price points, including less costly pricing. And, if you look at demographics of the country, things are pretty uneven. Some parts of the country are expecting significant declines in enrollment; others will see enrollment grow extremely rapidly. The potential for significant change is as high as it has ever been."

"This is not a recession from which we return to business as usual," says Currie. "Things will, in fact, be different."

At Franklin & Marshall College in Lancaster, Pennsylvania, President John Fry explains that the through-cycle approach has dominated his recession-fighting plans. "We have an extremely healthy, strong institution that has been on a very positive trajectory for a number of years," he says. "This recession created an opportunity for our team to move Franklin & Marshall more rapidly forward during a time of chaos in the market."

For example, the college is currently in the process of increasing faculty size by 40 tenure-track positions, which is a little more than 20 percent. "This is a very good market [in which] to hire talented junior faculty," Fry explains. "So while people are hunkering down, we're hiring because the talent is there and our needs are clear. I know that in three years or whenever we come out of this recession, we're going to have a great group of new faculty and that's going to put us further ahead."

In addition, the institution is undertaking a pilot three-year degree program option for qualified students who have the academic ability to work faster and harder than the typical four-year graduates. "In response to this unsettling economic environment, some students and their parents need to move through the Franklin & Marshall experience a little more quickly," Fry says. "We also have students every year who take additional summer courses or use the January break to pick up a credit. Why not structure a program to help them get through in three years?" According to the college's estimates, the compressed-degree program saves about 18 percent of the total cost of a college education. "That's real money," says Fry.

In addition to these through-cycle steps, the institution has outsourced computer procurement and servicing, consolidated purchasing contracts, renegotiated vendor contracts, and eliminated selected staff positions.

"Everything we did was based on an analysis of certain areas of the college that we felt should perform better or weren't as important as other areas we wanted to protect," Fry says. "We took a very surgical approach, eliminating some highly compensated positions, being careful to work with the affected individuals so they had time to look for other jobs, and providing references." Fry describes the approach as "tough-minded but humane." He adds, "The thing we decided not to do in the first year of this disruptive economic environment was to go across the board with freezes in compensation, on the theory that the changes we have seen in the economy are actually going to last a long time, and we need to protect our best performers."

SCRUTINIZING COSTS

Dean Currie, vice president for business and finance, California Institute of Technology, Pasadena, also opted against freezing compensation. "We didn't do any of the

APPLY MULTIPLE METHODS

How institutions are weathering the economy depends on many factors, such as revenue mix and cost history, observes Paul Jansen, director emeritus, McKinsey & Company. "A very well-endowed private institution will have a different set of issues than a state-funded public institution or a midtier institution that is highly tuition dependent. There isn't a one-size-fits-all strategy. The issues are very different across institutions."

In Jansen's opinion, institutions are employing one, two, or all three of the following strategies to survive the current economic upheaval:

- o **Bridging the crisis.** This is a short-term option for leaders who want to avoid painful cuts and who believe their budgets contain enough flexibility or fat to tough out the turmoil. If the recession stretches out, they have contingency plans to fall back on.
- o **Using the crisis.** Sometimes referred to as "don't waste a good crisis," this strategy can be used by business officers to reset costs, sometimes at significantly lower levels, and to take on a few of the institution's sacred cows. "In this strategy, leaders take an aggressive position early on because they don't know how long the crisis will last and they really want to use everyone's sense of urgency to make changes they might not otherwise be able to make," Jansen says. "A good number of institutions are adopting variants of that approach."
- o **Adopting a through-cycle mind-set for handling the crisis.** Building on the crisis strategy, business officers who adopt this approach invest in their institution's future. According to Jansen,

smoothing mechanisms," he says. "We didn't do hiring or salary freezes, and we didn't do borrowing. We didn't do one-time savings in the budget. Instead, we immediately asked, 'How can we permanently change our cost structure?' We began to rapidly pull together and say, 'Let's cut everything until the next cut would make us no longer CalTech.'"

By February, the institution had slashed its unrestricted budget by 10 percent and laid off 10 percent of its nonresearch staff. "Certainly the hardest part of doing something decisive is laying people off in a terrible economy," he admits. "After we finished what we hoped would be the last set of cuts, the feeling on the campus was no longer fear. Interestingly, it wasn't bitterness either. The feeling here was grief. We felt grief for the programs we lost and grief for the people we lost."

To overcome the outpouring of emotion from the layoffs, Currie made sure to communicate as much as possible, while the institution created areas on the edge of the campus where former employees could use computers, search for jobs, and meet with their colleagues. "We staffed these sites with our most upbeat HR people," says Currie. "Our attitude was to tell people they didn't do anything wrong. It wasn't their fault they were losing their jobs or their programs were being cut."

Despite these layoffs, the institution continues to seek out and recruit research staff. "At CalTech, our core strategy is to hire the smartest research people we can possibly find in the world and support them in doing something important. We will wait a decade to make an offer, and we'll try to recruit particular people whether or not they think they know they want to come. We're not always successful," he says, "but of our last nine offers, we've had nine acceptances. That's how you emerge stronger from an event like this. You continue to invest in your core strategy."

RUMOR VS. REALITY

Particularly in times of trouble, institutions need to emphasize communication, Olsen says. "We all want to be relevant to our stakeholders, regardless of the type of institution. We need to make it clear to our stakeholders exactly what we do, why we do it, and how we do it."

Fry believes that business officers often underestimate the ability of key constituents to understand the problems faced by senior administrators. "I have found repeatedly, without exception, that when I talk to the faculty and staff about what's really going on, the kind of response I get is, 'Thanks for telling me and giving me the facts. Now what can I do to help?'"

"Trust and have confidence in the people you work with, share information, and engage the entire community," advises Fry. "Don't take this on yourself. Don't be the lonely person in the corner office, puzzling through this and then issuing edicts. Make this what it is—a communitywide discussion about an institutionwide set of challenges."

Fry admits the through-cycle mind-set would never have worked without the full support of his college community. "I can't tell you how many town meetings and faculty meetings I ran, going through our income statement and enrollment projections, explaining our short-term tactical bridging interventions, and talking to everyone from groundskeepers to senior administrators to tenured faculty and

they say, 'We'd not only not waste a crisis, but we're going to invest in some areas. We are going to take advantage of the weaknesses of our competitors—however we define them—to reach target student groups, bring in talent in a way we might not have been able to in the past, or create new product lines, such as online learning, that position us to be very successful when we come out of the recession.'"

FOUR SCENARIOS FOR RECOVERY FROM RECESSION

How should colleges and universities prepare for the aftermath of the current recession? That could depend on what path you think the recovery will take. In early November, NACUBO conducted a poll of chief business officers, asking their opinion about which of four scenarios they think is most likely to occur. The scenarios are:

- o **A relatively quick recovery.** Policy makers succeed in generating sustained economic growth by the end of calendar year 2009.

trustees about our financial condition, our prospects, and the issues we're facing. There is a prolonged recession through mid-2010, and below-average growth through calendar 2012.

In mass communication and face-to-face discussions, Currie urges business officers to be as transparent as possible. When he teaches a course on university finance, he encourages both students and staff to ask questions at the end of the semester. "If it's not about an individual salary, I'll give them an answer," he says. "There is no reason for us to have secrets. Candor is a good strategy. People can deal with it. What they don't like is uncertainty."

SEEING IT THROUGH

Besides the importance of communicating candidly with stakeholders, business officers interviewed for this article offer several other strategic suggestions.

- o **Take action.** Don't hunker down and try to wait out the current situation. "These are challenging times for everybody, but we need to actively engage in addressing the issues," Olsen says, "and find a strategy to succeed. If the potential solutions we've learned throughout our careers are no longer available to us, we have to look at new and different ways of doing things. We may have to make changes that will leave our institutions different but stronger."
- o **Plan for all scenarios.** Model the "truly scary," advises Jansen. "Think about all the scenarios for how this may play out, not just the one you hope for," he says. "Make sure you have action plans appropriate for all of the scenarios you envision."
- o **Be bold.** "What would position your institution to succeed post-recession?" Jansen asks. "Be courageous. For example, if you know you have to expand geographically, a great time to buy real estate is during a recession. Prices are way down; you have distressed sellers. Being too cautious could cause institutions to miss a once-in-a-generation opportunity."
- o **Stay nimble.** Business officers need to adopt a more flexible decision-making and operating model. "The days of 'Well, we'll study this for six months or a year and maybe we'll take action—or maybe not' should be replaced with a much more flexible and quick decision-making process," Fry says.

Currie concurs, advising against a long, drawn-out period of cost cutting. "Rather than cut 5 percent this year and 10 percent next year, just do what it takes," he says. "Even though spending models may indicate such an approach, organizations are not built to live in fear and anxiety for that long a time. Have the discussion, make your decisions, and adjust accordingly."

- o **Concentrate on your mission.** There's nothing like a recession to help you focus on the essentials, Currie says. "Make whatever sacrifices you need to make so you can keep investing in your core value. Go back to your core strategy and throw away everything that

There is a prolonged recession through mid-2010, and below-average growth through calendar 2012.

- o **Modest recovery but stalled growth.** A recession of one or two more years is followed by below-average growth for the foreseeable future.
- o **Recession lasting for five years or more.**

Sent by e-mail to a random sample of 600 NACUBO primary representatives, the survey generated a 32 percent response rate. Respondents represented the following constituent groups:

Small institution.....	52.1%
Community college.....	17.2%
Comprehensive/doctoral.....	15.1%
Research institution.....	8.9%
Governing board.....	6.8%

Responses (with a plus or minus 5 percent margin of error) from all constituent groups followed the same pattern, so are grouped together in the attached figure. In comparison, the figure also shows responses to the same scenarios from a survey of international business CEOs conducted last spring by McKinsey & Company.

An additional nearly 6 percent of the NACUBO respondents chose "other" as a scenario and sent their own projections. These ranged from very pessimistic ("recession of three years followed by little growth") to quite optimistic ("the recession is over-growth will be slow through mid-2010-economy will take off in the second half of 2010").

Other scenarios included the following:

- o "Assume that we are at the middle point of a 'W' recession and will have another fall before an upswing."
- o "Health care and cap-and-trade pass and we enter into a new long-term recession with no growth."
- o "Above-average growth short term, but will fall back to stagnant or below-average growth for the next two years or so."

doesn't help you get there."

Jansen agrees. "Recessions create both pressures and opportunities. Think 'through-cycle' and anticipate the continued evolution of higher education to inform those long-term investments you want to make."

MARGO VANOVER PORTER, Locust Grove, Virginia, covers higher education business issues for *Business Officer*.

Copyright © National Association of College and University Business Officers. All rights reserved.