Borrowing during a time of crisis: Executive summary

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Although a great deal of attention is paid to student debt, colleges and universities have increased their institutional debt substantially over the past several decades. Institutional borrowing is an important tool colleges can use to meet strategic goals. However, when unchecked or done irresponsibly, institutional debts can undercut a college's ability to adequately serve students. Ithaka S+R conducted a mixed methods study, with the generous support of the TIAA Institute, to better understand how institutional borrowing decisions are made during periods of crisis, including the COVID-19 pandemic and the Great Recession. By better understanding how these decisions are made and the potential impacts of crisis-related choices, we hope to inform decision making around debt during future crises.

Our findings suggest that colleges and universities are more resilient than many voices in the field or media reports might suggest. While some have made grave predictions around financial downturns and colleges' ability to survive, our study revealed that chief financial officers (CFOs) are keenly aware of the risks of economic downturn, able to act swiftly to address financial threats, and carry lessons forward from previous crises (e.g., the Great Recession). In fact, after addressing the immediate concerns, CFOs often leverage these periods to improve the financial standing of an institution through strategic debt decisions. However, for some institutions, especially those that have faced historical public divestment, the financial burden during periods of crisis may be overwhelming and force colleges into debt markets in order to make ends meet. Below, we provide background information about university debt decisions, an overview of our study approach, a summary of qualitative findings from interviews with CFOs, and a summary of estimates on the impact of borrowing during the Great Recession. We conclude with implications for institutional leaders, policymakers, and researchers.

What is institutional borrowing?

Institutions primarily borrow funds for capital investments on campus. This may include building new labs and educational facilities, sports arenas, or dormitories. The array of projects reflects the variation in goals of individual colleges as well as across institutions.

When colleges approach the borrowing decision by weighing the benefits of issuing debt with using internal funds, they are seen to be following a static-trade off approach. For institutions following this approach, debt is part of a set of strategic tools used to reach financial and mission-related goals. These colleges often invest in projects that will provide revenue returns to offset the cost of the debt in the form of room and board, ticket sales, or increased enrollment.

Other colleges try to avoid debt and prefer using internal funds to pay for projects. These institutions, which are said to be following a pecking order approach, see debt as a last resort. Rather than taking on the risk associated with future revenues being able to pay off the debt, these colleges may forgo strategic capital investments until internal coffers or fundraising can support the project.

Regardless of which strategy an institution takes when approaching debt, the CFO is one of many stakeholders involved in issuing debt. Typically, decisions need to receive approval from other key internal stakeholders (e.g., the president and board of trustees). At public institutions, new debt may require the public to vote on a referendum or for the legislature to approve the decisions. Finally, a slew of actors in the financial service industry are involved in underwriting, packaging, and selling the debt to investors.

Once a college issues a debt and pays for a capital project, it assumes the risk of being able to repay that money, which may hinge on the success of a project. For example, many institutions need debt to build new dorms, and future room-and-board payments will help pay back the loans. In this way, the debt decision is both a current and future decision that must align with the strategic and financial goals of an institution. And while most debt is beneficial for colleges, some institutions may be over-speculative when borrowing (e.g., assuming there is enough student demand for a new dorm) or forced to borrow due to their financial circumstances, both of which can have dire consequences for a college and even force it to close.

What did we study?

In this mixed methods study, we examine the borrowing decisions during periods of crisis. The broader literature suggests that most colleges borrow to meet strategic goals and those with more resources follow a static trade-off approach that helps them use debt to meet these goals. However, colleges that borrow out of desperation or when their financial futures are uncertain often face difficulties repaying debt. As such, we explicitly look at the borrowing patterns and decisions during periods of crisis that may destabilize institutional revenues or create uncertainty. The lessons learned from these periods can help inform approaches to future challenges.

First, we conducted descriptive analyses and event study analyses to identify patterns in borrowing during the Great Recession. Our goal was to better understand how the Great Recession affected borrowing patterns across institutional characteristics, and if those patterns were associated with positive or negative institutional outcomes. To this end, we first identified characteristics associated with increases in total debt, debt per full-time enrollment, and leverage.

We then focused on institutions that increased borrowing significantly during the Great Recession and identified the institutional characteristics associated with this growth in debt. We used a difference-in-differences and difference-in-difference-in-differences approach to understand how large increases in borrowing related to long-term educational expenditures, and how these relationships vary across institutional characteristics. Our approach does not provide causal estimates of the impact of borrowing but does elucidate important longitudinal relationships.

Informed by our quantitative analyses, we purposefully sampled CFOs from institutions with varying levels of debt, in the public and private sectors, with variable Carnegie classifications and mission orientation, and with and without an HBCU designation. We conducted hour-long interviews with eight CFOs where we asked questions about the borrowing process generally, the decision-making process during COVID-19 and the Great Recession (when possible given the tenure of the CFO), and the implications of borrowing decisions. These interviews provided new insights into borrowing and contextualized our quantitative findings.

Who borrows during a crisis and why?

We found large differences in borrowing across institutional characteristics. For example, research institutions borrow more in both absolute terms and per FTE calculations than their peer institutions. Private institutions also have significantly more debt than public institutions. And while private institutions are subsequently more leveraged than public colleges, the gap has closed over time. We also identified an important trend among HBCUs. HBCUs borrow less than non-HBCUs, and the patterns remain relatively constant over time. However, after the Great Recession, HBCUs became significantly more leveraged than non-HBCUs, suggesting that these colleges may be borrowing for different reasons or may be facing other market pressures that are impacting the value of their assets or revenue. These initial descriptive analyses indicate significant heterogeneity across institutions in borrowing patterns. This variation helped inform our subsequent quantitative and qualitative analyses.

Our second phase of quantitative work revealed that HBCUs and public institutions were significantly more likely to increase debt during the Great Recession. Our modeling approach is detailed in the full report, but it is worth noting these findings were robust to numerous specifications. This growth may be related to both the immediate financial circumstances of these institutions and the historic divestment. During the Great Recession, states faced significant budget shortfalls, and higher education was frequently at the top of the list of things to be cut. Historically, HBCUs have faced severe underfunding. For both public institutions and HBCUs, these funding shortfalls may have contributed to a need to engage debt markets when other revenue sources were insufficient. It is also important to note that HBCUs serve students with more financial need than peer institutions, on average, and the Great Recession disproportionately impacted labor market opportunities for Black individuals, thus exacerbating the financial need of Black students. These broader forces may contribute to the overall financial health of an institution that relies on tuition revenue and has limited financial aid resources, thus impacting borrowing decisions. Qualitative interviews suggest that some HBCUs may borrow out of necessity during periods of crisis because of their financial precarity. For these institutions, debt becomes a lifeline to stay afloat during difficult times.

Our quantitative findings also suggest that pre-Great Recession leverage was inversely related to the likelihood of increasing debt during the Great Recession. That is, colleges that were highly leveraged before 2008 did not take on even more debt during the economic crisis. This finding reflects a prudent approach to debt management and provides reassuring evidence that for many colleges, an economic crisis does not necessarily force them to make potentially risky decisions.

Our interviews with CFOs also found that during COVID-19, many campuses paused capital projects and halted borrowing while they assessed the potential financial implications of the crisis. However, upon seeing enrollments remaining steady or not falling as much as expected and receiving an influx of federal aid, CFOs saw the low interest rates as an opportunity to improve an institution's financial position. Some CFOs refinanced debt to lessen the annual debt servicing costs, thus freeing up more funds on campus for other expenditures. Others used the low rates to shorten the lifespan of current debt obligations. This strategic engagement of the debt market suggests colleges, after grappling with the immediate needs of a crisis, use the tools available to plan for the future and improve their long-term financial health and market positioning.

Is borrowing during a crisis a good idea?

Our quantitative findings suggest that, overall, colleges that increased debt during the Great Recession likely did so in a strategic way. For colleges that borrowed irresponsibly or out of necessity, the future cost of that debt would likely impact a school's ability to serve students. To examine this relationship, we look at how education and related (E&R) expenditures change over time at institutions that did and did not increase debt significantly during the Great Recession. We found that E&R expenditures increased over time at high-borrowing institutions, suggesting these debts did not undercut institutions' ability to serve students.

As reflected in our qualitative interviews, CFOs approach debt cautiously, and those that engage in debt markets during periods of crisis are likely doing so in a strategic manner. Lessons learned during the Great Recession have carried forward into future planning. Several CFOs discussed how the response to COVID-19 directly reflected the positive examples from the Great Recession. Colleges learned to have sufficient cash on hand to cover immediate needs, such as payroll, and to have a plan to halt capital projects. Not only were learned behaviors carried forward, in one instance a CFO has kept an emergency line of credit open since the Great Recession in case it ever becomes necessary again. Some CFOs that used the low interest rates during COVID-19 to improve the financial health of an institution directly reflected on "missed opportunities" during the Great Recession to make similar moves, in part because institutions were less prepared in 2008.

Although large increases in borrowing during the Great Recession appear to be unrelated to institutions' ability to serve students, on average, we conducted more detailed analyses that sought to understand if this held true across institutional characteristics. At HBCUs and public institutions, the share of total expenditures spent on education and related expenses decreased in the long run for institutions that significantly increased debt during the Great Recession. At public institutions, however, there were significant increases in the total and per FTE E&R spending, which suggests that the debts may be contributing to an overall budget expansion where E&R expenditures are a decreasing share of that new budget.

At HBCUs, however, we do not find any significant effects on increases in total or per FTE E&R spending. This suggests that colleges that increased debt significantly during the Great Recession may have done so out of necessity or have made imprudent investments that subsequently affected their ability to serve students. Our interviews revealed instances where HBCUs borrowed during the Great Recession in order to make payroll and keep the lights on. While this type of borrowing may have been necessary to keep the institution financially solvent in the near term, it is unlikely to position a college for long-term success.

How do these findings impact institutional and public policies?

Our study highlights the importance for colleges to have plans in place to manage debt, and finances more generally, during a period of crisis. Some lessons learned from the Great Recession were carried forward to COVID-19, and it behooves CFOs to carry new lessons forward to future crises. For example, positioning a college to avoid having to borrow out of necessity during a crisis is an important step for ensuring the long-term health of an institution. Additionally, CFOs should consider how periods of crisis can provide opportunities to lower debt obligations and reduce the long-term risk associated with previous borrowing. During the pandemic, many CFOs we spoke with took advantage of low interest rates to restructure debt rather than increase debt to fund new capital projects. A conservative approach to borrowing is likely to be beneficial for the long-term health of colleges.

We uncovered important relationships between institutional characteristics and borrowing practices and outcomes. During the Great Recession, public institutions and HBCUs were more likely to increase debt significantly. HBCUs have historically had fewer resources than predominantly white institutions, and public colleges faced significant cuts to state funding. While we cannot make causal links between funding and borrowing, the association between the two is concerning and worth additional research. Additionally, ensuring these institutions are appropriately funded may limit borrowing out of necessity and allow institutions to borrow more strategically. The federal government should continue to identify ways to invest in HBCUs and consider identifying mechanisms that incentivize states to adequately fund public colleges and universities.

Finally, debt is an important factor in the long-term financial health of an institution, which affects current and future students, and colleges' ability to properly serve them. While the Department of Education uses a set of financial oversight metrics, research suggests these may not be effective at predicting institutional closure or distress. Alternatively, accrediting organizations generally include financial oversight in their review of institutions. We believe these organizations are uniquely positioned to monitor borrowing decisions and contextualize them within the overall goals and health of an institution. Additional research to understand the effectiveness of accreditors overseeing institutional finance would help inform oversight mechanisms related to debt that ensure responsible borrowing.

About the authors

James Dean Ward is a senior researcher at Ithaka S+R on the Educational Transformation team. His work focuses on federal and state higher education regulatory, funding, and financial aid policies. James earned a BA in economics and history from Cornell University and a PhD in higher education policy from the University of Southern California. James has published and presented work on state financial aid programs, performance-based funding policies, for-profit college regulation, institutional finance, and equity in postsecondary opportunities. In addition to serving as a research assistant in the Pullias Center for Higher Education, James was a postdoc research fellow at the University of Southern California. Prior to graduate school, James conducted research on postsecondary finance at the National Association of College and University Business Officers and served as an institutional researcher at Harvard University. As a higher education consultant for ASR Analytics and Hanover Research, he worked on projects related to institutional aid policies, program development, admissions and recruitment practices, and institutional economic and community impact.

Mya Haynes is an analyst on Ithaka S+R's Educational Transformation team, where her research predominantly focuses on college access and success for lower-income students. Prior to joining Ithaka S+R, Mya interned at the American Civil Liberties Union, where she co-authored a policy research brief and evaluated the National Advocacy Institute—a summer program engaging youth in advocacy and activism. Mya holds a master's degree in higher education with a concentration in public policy and a bachelor's degree in sociology, both from the University of Michigan. Her research experiences as an undergraduate and graduate student centered around student success for Black and first-generation college students through mixed methods studies.

Staci Gusakova is former Ithaka S+R intern who researched institutional borrowing alongside James Ward. Currently, Staci works as a User Experience Research Associate at Google and conducts mixed methods research to make Google Search Ads more useful and trustworthy. Staci holds a PhD from the University of Michigan in Psychology and Women's and Gender Studies. During her PhD, she researched what factors help people maintain high quality relationships over time, with a specific focus on issues that disproportionately affect gender, racial, and sexual minorities.

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