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OPINION

Bubbles 101

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Bubbles burst when the market suddenly recognizes a disconnect between price and value. In 2003, this was caused by Internet companies' failure to convert from "mind-share" and eyeballs to revenues. While the recent economic crisis was due to many factors, certainly one was the extensive house of cards built on mortgages. Be prepared for new models that shake up the economics of higher education.

When we think about financial bubbles, we typically recall the recent run-up in house prices or the dot-com craze of the late 1990s (and some think of the 17th century tulip bubble). We might define "bubbles" as sharp price increases for an asset without supporting increases in the intrinsic value or other fundamental financial characteristics. Another defining feature: You can't see a bubble until it pops.

College education seems to be heading in that direction. The College Board reports that tuition has increased on an inflation-adjusted basis by 6.6 percent at public universities and 3.2 percent at private schools.

While proponents argue that these increases are mitigated by a broad suite of financial aid, Pell Grants and other programs also effectively boost tuition costs to everyone else, as the Cato Institute's Neal McCluskey has clearly explained.

To make matters worse, with 55 percent of bachelor degree's recipients at public colleges borrowing an average of nearly US$20,000, it is clear that we are launching a generation of debtors.

Online Education, Digital Texts

Is the rapid price increase a response to skyrocketing costs? Hardly. The key expense to universities is faculty salaries, and the Chronicle of Higher Education reports that salaries rose by only 1.2 percent this year. In fact, costs are likely going to plummet as universities experience the same massive restructuring affecting every other industry.

As I discussed in this space earlier this year, college professors are outsourcing grading overseas, according to the *The Chronicle of Higher Education*. Even if this option only replaces low-cost graduate teaching assistants, it still represents a decreased expense.

In addition, universities can reduce costs by exploiting new online systems. The Sloan Survey of Online Learning reports that online enrollments grew by nearly 17 percent, dwarfing the 1 percent increase in the number of enrolled costs.

More than 25 percent of enrolled college students now take at least one course online. (It is interesting that less than 1/3 of the chief academic officers believe that their faculty recognize online education as legitimate.) A similar development is the fast proliferation of digital textbooks. The overall cost associated with educating a student is thus likely falling.

Price-Value Disconnect

Another red light on the bubble-ometer is the fawning over the leadership managing the price increases. From Jeffrey Skilling at Enron to Angelo Mozilo at Countrywide, each of our recent dramatic run-ups has been marked by effusive praise of the CEO-cult leader. *The Chronicle of Higher Education* reports the dramatic increase in college presidents with compensation exceeding US$1 million (see the Daily Beast for details on the top earners).

So the price is skyrocketing, the cost structure is falling, and compensation for leadership has reached unprecedented levels for that industry. Does the price increase reflect improved value? On one hand, *The New York Times* has reported that the 2009 unemployment rate for college graduates was half that of those limited to a high school diploma, and that the median income was substantially higher.

However, with an estimated payback time of 11 years for the lost time from the workforce and a loan for a degree from a public university, this represents a significant investment. Furthermore, *The New York Times* separately showed that of the 30 jobs projected to grow fastest in the United States, only seven require a college degree; most of the jobs with higher demand -- registered nurses, home health aides, and customer service representatives -- can be done with lower levels of education.

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2003, this was caused by Internet companies' failure to convert from "mind-share" and eyeballs to revenues. While the recent economic crisis was due to many factors, certainly one was the extensive house of cards built on mortgages. Be prepared for new models that shake up the economics of higher education.

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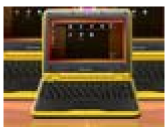

The continued growth in cloud adoption may radically change netbook adoption rates. "As more organizations explore a virtualized desktop and cloud-based productivity options, the netbook could be an interesting conduit to a world featuring 'Everything as a Service' -- providing traditional I/O to enable productivity tasks, but at a lower-cost, more portable profile," explained Deloitte analyst William Briggs.
