Panel: Racial and Economic Equity in Higher Education

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The Market, the American Dream, or Dreams of the Lottery
The Robert H. Atwell Plenary Address
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Ithaka S+R provides research and strategic guidance to help the academic and cultural communities serve the public good and navigate economic, demographic, and technological change. Ithaka S+R is part of ITHAKA, a not-for-profit organization that works to advance and preserve knowledge and to improve teaching and learning through the use of digital technologies. Artstor, JSTOR, and Portico are also part of ITHAKA.
Economists have a bad reputation, which I think is mostly undeserved (as Ted mentioned, I am one myself!). This bad reputation arises for a variety of reasons, with some thinking the field is boring (the dismal science rap). Trying to decide whether to attend this event today, a journalist friend asked me if my talk was going to be boring (I guess you are going to find out!). In addition to being boring, many also believe economists only care about and/or are good at making money, the “economists know the price of everything, and the value of nothing” rap. I don’t think either of these criticisms of economists is fair or true. But, I do think the bad reputation partly results from our liking markets. We do tend to like markets, because in many cases they allocate resources efficiently. Under a set of specific conditions, markets produce the lowest cost and highest quality things that people want to buy, which makes people better off, despite the negative reaction to the words “markets” and “efficiency” particularly in higher education. We are all usually better off if we can buy the things we want or need at the lowest price and at the highest quality (with some important exceptions). But, most economists think of markets as a means to an end, and not an end in themselves to be intrinsically valued or worshiped. And, many of those who do indulge in market worship, I would argue, aren’t very good economists, or even economists at all.

Instead, economists understand that under a variety of conditions markets don’t work well. Either regulations on those markets or non-profit or publicly supplied goods and services will do a better job of meeting people’s demands for a wide variety of goods and services, which again, in turn makes people better-off. Markets work some of the time, even often. But not always.

One of my favorite books that makes this all clear is by Arthur Okun, a book titled *Equality and Efficiency* published in 1975. Arthur Okun was a faculty member at Yale and chair of the Council of Economic Advisors in the late 1960s. I highly recommend the book. In just 120 pages, it will restore your faith in economists, if perhaps not our society! In addition to explaining the benefits of markets, Okun talks convincingly about several transactions that should not be allowed to be traded in the market, including

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1 A video of the original presentation at ACE 2019 is available at https://www.youtube.com/watch?v=TC-5xXh7ns&feature=youtu.be.

voting and military service. While Citizens’ United has undermined the notion that votes shouldn’t be bought and sold in America, at least a new election has been called in North Carolina in response to the quite explicit voter fraud there.\(^3\) In the case of military service, by eliminating the draft and going to an all “volunteer” military, we’ve moved military service into the market, which I’ll return to in a bit.

One obvious limitation of markets is that they don’t have anything to do with what we call initial conditions. Some people, for example, make their way through life with close to half a billion dollars in wealth inherited from their father, which puts them in a very different position as they operate in the market economy from, say, your average African American families, who according to the Pew Research Center have only about $11,000 in accumulated wealth.\(^4\) It is a little hard to conclude that the operations of the market, given these initial conditions, are fair in any way. So, income inequality and the distribution of wealth are things that a society might decide to not let the market completely decide. Progressive tax policy and government expenditures can moderate the effects of the market on members of a society, for example. To what extent is, of course, a political decision, but it involves Okun’s key idea, the tradeoff between equality and efficiency.

So, initial conditions are important, and it is important to remember that the operation of today’s market economy creates tomorrow’s initial conditions, which may or may not be considered fair for the next generation.

Let’s talk about the American Dream. Our society has long been committed to economic and social mobility. At first, of course, we meant this was an opportunity for white, Protestant men, but the population for whom we aspire to offer equal opportunity has grown over time to be significantly more inclusive. And, in the 21st century we still believe education is a main way of supporting equal opportunity, and the idea that anyone can succeed if they work hard. At the same time, education is one of those services that we over time decided shouldn’t be supplied through the market. First primary schooling and then secondary schooling were supplied by the public sector to all children for free, regardless of their parents’ incomes. While there remain significant inequities in the quality of such schooling across communities, access is guaranteed. And, recognizing the importance of pre-school, communities are moving to make this more readily available through the public sector as well.

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Post-secondary education—college and university education—has traditionally been supplied in the US for at least a century and a half through private, non-profit, or public colleges and universities, again in recognition that for-profit firms might not adequately supply it. The arguments for this are basically that the assumptions that lead to for-profit firms efficiently supplying goods and services—highest quality and lowest cost—are not met.

One justification for government involvement in higher education is “positive externalities,” with higher education contributing to knowledge, economic growth, greater community engagement, better health and participation in our democracy through voting. These are things individuals might not take into account when deciding how much to invest in their own education. While higher education clearly involves private returns (like higher lifetime earnings), these positive societal returns mean that too little investment would take place without some form of government intervention.

Higher education is also a complex good with the benefits accruing over very long periods of time, and in most cases will only be consumed once by each student. These characteristics make it difficult for students and families to assess the quality of the services they are purchasing, reducing the power of the market to encourage quality at the lowest cost, which would happen with a repeat purchase of a simpler good, like a cup of coffee. If the coffee isn’t very good and/or too expensive, people will vote with their feet and that coffee shop will go out of business.

Of course, over the last several decades, the for-profit sector in higher education has expanded rapidly, and economists who understand the limitations of markets are not surprised by some of the resulting problems. It is interesting to ask why these for-profit institutions have been able to thrive recently, but didn’t earlier in the 20th century. Part of the explanation is that the for-profits have been able to compete now because barriers to entry have gone down. Many public and private, non-profit colleges and universities have raised tuition and decreased their subsidies because of decreasing public support. When tuition was free or very low and subsidies larger, it was harder for firms looking to make a profit to compete. Declining trust, resulting from a variety of developments, including increasing costs, inadequate efforts to evaluate what students are actually learning at college, and concerns about commitments to free speech have also contributed to for-profits being able to compete. But, predatory behavior on the part of

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many—not all, but many—for-profits suggests that the market failures in higher education justifying non-profit or public provision still exist and some form of government intervention is needed to protect students and their families. The for-profits face incentives to generate revenues to add to profits, rather than to improving educational outcomes.

At the moment, the existing private, non-profit sector in higher education and the public sector as well have proven inadequate at responding to the increased demand for education (and skilled labor) that we are seeing in the labor markets, in the United States and across the globe, and the for-profit sector has entered this vacuum but is not up to filling the gap. We need some changes to support non-profit and public colleges and universities and even the for-profit sector to more effectively contribute to increased educational attainment and equitable access in the United States.

One challenge is that the colleges and universities in the non-profit and public sectors, despite not being located in the private for-profit market economy, are highly competitive with each other.

One challenge is that the colleges and universities in the non-profit and public sectors, despite not being located in the private for-profit market economy, are highly competitive with each other. They are a type of firm, even if not for-profit, and have objective functions that they maximize. A for-profit firm would have an objective function that mostly focuses on maximizing financial returns to owners or shareholders. For non-profit private and public colleges and universities, the objective function is more complicated and based on mission, not profit. That mission needs to be undertaken subject to a budget constraint however. If the institution wants to be financially sustainable, making money is not irrelevant and this also affects their behavior. These colleges and universities can in fact make profits and accumulate wealth, and some do. They just don’t have shareholders or owners to whom to distribute them. Mission is complicated. It could include educating undergraduates and graduate students, doing research on important issues, contributing to the local community, or saving for the future. For a variety of reasons, “excellence” has become a part of many institutions’ objectives—the best students, the best faculty, the most important research. While some blame this on US News and World Report (USNWR), I would argue that this commitment to excellence and the competition among institutions to be better than their
peers results from the interests of the constituencies of colleges and universities (faculty, the administration, students, and alumni), and because it feeds back into relaxing the budget constraints that all institutions face. USNWR reflects this, as much as causes it.

Because of this “excellence” objective, competition among colleges and universities doesn’t lead to the highest quality at the lowest cost. Instead, it leads to the highest quality at the highest cost that is sustainable over time by the institution, given its revenue sources. With rising income inequality in the economy, resulting from globalization, technological change, and decisions about macroeconomic policy on the part of the government, this competition for excellence has led to many of the problems that are confronting higher education.

Concerns about cost are real, but have resulted in large part from the increased returns to higher education and to rising income inequality over the last four decades, as well as the competition for excellence. Higher education employs a lot of people, and people with lots of education themselves. In labor markets today, those people command higher compensation, and this has contributed to rising costs in the sector, absent innovations to save on this expensive input—talented people. And, because of increasing income inequality, the incomes of many of the students and families seeking higher education have not kept up, making investing in higher education much more of a challenge.

Thinking that greater competition within the sector would help control costs as it would in a textbook situation, there have also been pressures for the sector (public and private non-profit colleges and universities) to be subject to greater discipline “from the market.” It was hoped that this would address concerns about rising costs, the lack of productivity increases, and rising tuitions. But, efforts to increase competition to control costs have actually had some unintended consequences.

An example is student course evaluations of professors’ teaching, a means of creating incentives for effective teaching, with students being the consumers who will impose the discipline of the market on the faculty who are supplying the services that they are purchasing. But, higher education has been in the public and non-profit space precisely because students may not be in the best position to evaluate the education they are receiving at the time they are receiving it. Moving in this direction—treating students as consumers—has created incentives to value student satisfaction, even if at the expense of educational value. Many students value being asked to work harder and wrestle with complex and uncomfortable ideas, but how many? And, how many like nice dorms, good food, and access to great fitness centers? As schools compete for students, expenditures may get shifted to greater consumption such as nice dorms and fitness centers and less to investments with greater educational value such as more full time professors and well-resourced libraries, particularly since the outcomes of those investments are harder to
evaluate. This homage to the market has actually decreased quality rather than increasing it.

Other examples exist. I’ll return to one in a minute.

What can be done?

There are some things we shouldn’t do.

The status quo probably is sustainable for a while and perhaps a long while, but is risky.

The rising income inequality in the economy has contributed to rising inequality in resources across higher education. As an example: Private non-profit doctoral institutions with the top 10 percent of students based on endowment per student spend on average about $92,500 per student per year on education and related expenses. Institutions with the bottom 10 percent of students spend $18,100. (That’s a ratio of about 5 to 1.) Comparable data for Baccalaureate institutions are $53,000 and $15,000 (for a ratio of about 3.5 to 1). Students are having very different amounts spent on them. And, of course, the community colleges are at the low end of resources spent per student, with little or no endowments.

It is the case that high endowments per student are positively correlated with lower net prices for lower income and middle income students, but not more lower and middle income students. So, schools with larger endowments per student are asking low and middle income students to pay less than their higher income peers, but they aren’t taking that many of these students.

I think all of this has contributed to the hostility against higher education on the part of much of the public, and has the potential for leading to bad public policy, as I would argue last year’s tax bill demonstrated. So, the status quo risks continued or increased hostility on the part of the public, and possible policy interventions that would do significant damage to the higher education sector, and the institutions that comprise it.

So relying on the status quo to continue is one thing we should avoid. Some other things we shouldn’t do:

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7 Sandy Baum, Catharine B. Hill, and Emily Schwartz, "College and University Endowments: In the Public Interest?" Ithaka S+R, May 22, 2018, https://doi.org/10.18665/sr.307377.
8 Ibid.
9 Ibid.
Free tuition proposals also have significant problems. If something is free, but not very good, it may not improve people’s welfare. There could be unintended consequences of free tuition, with students going for free over quality, when the more expensive option might have higher returns for them. If lower tuition for lower income students were combined with improved educational outcomes, which in most cases require some additional resources or a reallocation of resources, it would be a different story. In higher education, we often focus on the tuition or the price tag, without also examining what you are getting for that price, partly because what you are getting is hard to evaluate.

Ending legacy admissions and early decision at the subset of schools that do not have open admissions, and that instead reject a large number of their applicants, is receiving attention and also reflects the increased hostility toward this sector of higher education. While regaining the public trust is really important, I don’t see these changes as either necessary or sufficient for improving low and middle income access to higher education. These policies don’t have unintended consequences for low and middle income families: they have perfectly understood and intended consequences, which is to have an impact on the final matriculated student body, competing for those excellent students with the least impact on the budget constraint. Absent policies to increase need based aid, ending these policies make for good sound bites but not necessarily good public policy. Will welfare be improved if Stanford’s legacies attend Princeton instead? Or schools spend more resources on enrollment management services to yield the class within their financial aid budgets through regular admissions? Increased hostility toward legacy admissions and early decision has in part arisen, I think, from the fact that higher education is understood to be more important now than previously, and that the resources across higher education have become more unequal. This has increased the competition for seats at a set of institutions—those with the most resources making them increasingly selective—and this in turn increased the resentment for seats going to these special categories. Some add affirmative action and athletic admits to this list of admissions practices raising questions for the same reason.

So, instead, what needs to happen:

1) First, the better resourced colleges and universities (private non-profit and public flagships) that have benefited from the evolution of the economy over the last forty years need to do more to serve their missions and the public good, justifying their larger public subsidies. It is important to remember that these institutions receive significant public support (federal, state, and local) from grants, special tax treatment including exemption from income and property taxes and incentives for charitable contributions, as well as appropriations on the part of the publics. As I mentioned already, the status quo is risky, even if sustainable for some period of time.
Increased collaboration among these institutions would help counter the pressures of competition to push up costs, and the federal government needs to make this possible. Changes in public policy would help. Increased collaboration among these institutions would help counter the pressures of competition to push up costs, and the federal government needs to make this possible. Antitrust laws exist in America in recognition that the market will not always operate in the interests of consumers. There can exist conditions where monopolies arise, and monopolies will produce too little at too high a price in search of maximizing profits, because these monopolies don’t face any effective competition. Antitrust laws were used against higher education in the early 1990s, but in fact worked to hurt the public interest and consumers, rather than protect them. (This is another example of unintended consequences of increasing the role of the market in higher education.) Being subject to antitrust actions did increase competition among institutions, but in ways that hurt many students and families rather than benefiting all of them. While some gained, overall the system moved in a direction away from serving the public good.

As an example, take merit aid. In search of excellent students, and those who can contribute to relaxing the budget constraint because they can afford to pay something, schools moved toward awarding merit aid to attract a class that met these objectives. (An entire industry arose to help schools do this!) This benefits a set of students who receive the merit aid, but hurts the overall system, as resources are transferred to those who could afford to pay in many cases (although not all.) If one school offers merit aid, they can attract these students. If the school’s closest competitor does the same, the allocation of students may end up the same, but these particular often well-to-do students pay less and the schools have fewer resources for their educational missions. Is society better off? If those students would have and could have invested in their education anyway, and some lower incomes students absent the needed need-based aid, can’t and don’t, then they are worse off and the economy is worse off because talent is lost.

Education is one of those things that can increase both equity and efficiency. By investing in education, a society can improve the welfare of individuals and improve the

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capacity of the economy to supply valuable goods and services. But, it does need to be paid for.

While colleges and universities can work to reduce unproductive competition, relaxing the threat of antitrust action would facilitate this. With collaboration, institutions can do things that benefit them individually and collectively if collectively pursued, but could hurt them if they go it alone. Reducing merit aid or cutting back on amenities (such as high end dormitories) are examples. It should be possible to make distinctions among types of competition to identify those that harm the public good.

What else can we do?

2) Second, I want to return to the draft for a moment. In the 1970s, Arthur Okun argued that military service was obviously one of those obligations that should not be allocated by the market. Writing shortly after the end of the Vietnam War, understanding the fairness of a universal draft (even if some were able to get around it—foot issues that interfere with military service but not with playing golf come to mind) and perhaps also the role the draft played in mobilizing efforts to hold the government accountable for its decisions, this conclusion is taken as almost obvious. But, now with an all-volunteer military, we’ve given this “obligation” to the market instead. The military prefer this, since clearly working with those who have volunteered must be easier than with those who are serving unwillingly, and I suspect most families prefer this system too. But, it is clearly the case that it reduces the motivation for the broader public to scrutinize where we send our troops and for what purpose. I know I would have paid significantly more attention had my children been subject to a draft. Think about the political power of MADD and its ability to move the drinking age to 21, slightly ironic given the preference on our part for some other families’ children to “volunteer” at 18 and serve in places like Afghanistan, Iraq, and Syria.

“All volunteer” seems a bit disingenuous to me. Okun argues that voluntary trades under conditions of “extreme need” aren’t really fair trades. Is this the case with military service? Perhaps or clearly it is a bit of an overstatement, but many young people enlist because it is seen as one of their best options for getting an education. Their family incomes are such or their high school preparation is such, that they don’t see another path to higher education at age 18 so as to avoid a lifetime with only a high school diploma. Many of course do volunteer wholeheartedly and it is just what they want to do. But, the fact that those who “volunteer” do not come equally from across income and racial and ethnic groups suggests that other things, their initial conditions, are playing a role.
Given this, as a nation we owe these young men and women an education when they leave the military. Currently, veterans are overrepresented at the for-profits and underrepresented at colleges and universities with higher graduation rates. After World War II, institutions stepped up and opened their doors. Forty-seven percent of higher education admissions in 1947 were veterans. Even the women’s colleges (including Vassar College) opened their doors to men (although not their dormitories), when men couldn’t find seats elsewhere. By 1956, 2.2 million veterans had used the GI Bill to go to college. We should do the same now, but we aren’t. Why not? Because we don’t need to. The colleges and universities with the higher graduation rates and the most resources have plenty of applicants who are very talented, and many can pay the full tuition. We aren’t worried about another great depression as was the case as World War II drew to a close, nor fear the civil unrest that arose post World War I when veterans couldn’t find jobs. So, why risk admitting veterans? Because it would be the right thing to do, and we owe it to them in return for their service and in return for allowing so many other young men and women to go directly to college, without being subject to a draft. It would also have the added benefit of bringing to campus a diverse group of talented young men and women with very different life experiences, which would add to the education of all students. And, it would help counter the narrative of the better-resourced schools as elitist and excessively liberal. I hope some schools will take the lead on this. Many publics and community colleges are already doing a good job. The better resourced schools need to do their fair share.

3) Third on the to do list: As the higher education act comes up for renewal, we can also hope for better regulation. While I said that most economists don’t worship markets, there are some very distinguished ones who recognize that markets don’t always work according to the textbook, but that there is also significant government failure. Expecting the government to do better is naïve. (So, when you’ve finished Arthur Okun, turn to Milton Friedman’s Capitalism and Freedom.) We have plenty of examples of both good and bad regulation. But, striving for better regulations to me makes sense. I have faith that we can hold government accountable to serve the public good through our democracy, even if we don’t get it right all the time.

Better regulation could help the not-for-profit sector and the public sectors improve educational outcomes in a variety of ways. A change in regulations allowing greater

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cooperation would be helpful. It could constrain unproductive competition and channel those pressures toward better serving public objectives. Improved data reporting could encourage colleges and universities to adjust their policies and also give students and families better information on which to make decisions. (You may have noticed that some information has recently been removed from the College Scorecard, going in the wrong direction!)

Better regulation of the for-profits is clearly needed. Here is an example of significant government and regulatory failure. Regulation has aided rather than constrained, the market failures affecting the for-profit sector. The Department of Education’s deregulation campaign is a perfect example of failed public policy. It has aided and abetted the predatory behavior of many of the for-profits, again many not all, and our veterans are a major casualty of these policy failures. Not only does the 90/10 loophole remove a very small market constraint on the for-profits in taking advantage of veterans, but many in the current Department of Education formerly worked for the for-profit sector and probably will again, a classic example of regulatory capture. Ideally, the numerous veterans and military service organizations will get the word out to their constituencies and counter the for-profits’ recruiting success and decrease the demand on the part of veterans for their services. But, greater seats in better alternatives—the high graduation rate not-for profits and the publics—would help. Wouldn’t it be great if they were recruiting veterans as actively and effectively as the for-profits?

4) Fourth on the to do list: Those with resources should consider growing their class sizes and serving more students. I know all the arguments against this and have made them myself over the years, and they are convincing for any one institution. I’ve written the memos that make the case that growing reduces endowment per student and reduces the ability to compete with other institutions on quality. But these arguments are based in institutional objectives, and not necessarily the overall public good. Growing would be a way of reallocating resources across students, if not across institutions. Let more students benefit from the resources of the wealthiest schools—not just their endowments and their physical assets, but their academic programs and alumni networks. And, it would make the competition for seats at the selective schools less of a zero-sum game, which is a source of some of the current hostility that I’ve mentioned. When many

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13 The Department of Education has removed national data from the individual school data reports, making comparisons more difficult. See https://collegescorecard.ed.gov.

institutions went coeducational in the 1970s, they grew to avoid the pushback from alums on reducing seats for their traditional pool of students, whether men or women.

Those with resources should consider growing their class sizes and serving more students.

There are so many committed colleges and universities, in addition to the ones I’ve mostly been talking about that are working incredibly hard to improve student success. I’d love to see greater resources across higher education, particularly for those with the least wealth including community colleges, rather than reallocating resources among institutions. But in the current environment with the current disparity in resources available to students, we risk the latter.

Now it is time to talk about lotteries. Our national narrative is that anyone can succeed if they work hard. Americans have been very tolerant of income inequality, believing in equal opportunity and economic and social mobility. Income inequality has been accepted, in part, because families value the possibilities and rewards for themselves and their children of climbing higher on the income ladder. They believe they have a fair shot, if they work hard. But this tolerance is being tested because of the rising levels of inequality combined with the challenges of access to higher education particularly for low and middle income students, and this path to economic and social mobility seems more of a dream—winning the lottery—and less of a real possibility through hard work and determination.

At the same time that the path to economic mobility through education has become more challenging for many, there is an increasingly loud narrative that students are borrowing huge amounts to go to college and then being saddled with debts that they can’t repay, and that there is no need to go to college—one can make it in America without a college degree. Look at Bill Gates and others. Peter Thiel—the Pay Pal billionaire—offers students a scholarship for NOT going to college. This from someone with two post-secondary degrees from one of the most selective and wealthy institutions in the US, and three passports by the way, reducing the link between his and our nation’s welfare. Fortunately, I think there are only 20 of these scholarships a year, but the message that you don’t need to go to college to do well in our economy is so misleading. All the evidence suggests otherwise.

We shouldn’t replace a commitment to the American Dream with dreams of the lottery. The best path to social and economic mobility and an improved life trajectory is through education. Our colleges and universities need to work harder to improve the opportunities that our increasingly diverse population face and our public policy makers need to stop bashing higher education and work with colleges and universities to improve the lives of those who make up our country. Many of the challenges facing higher education are the result of policy makers not adequately addressing increasing income inequality in our society and its implications. While higher education institutions cannot address rising income inequality on their own, they need to more intentionally avoid giving the public sector reasons to bash them. Doing as much as possible to serve the public good will help restore trust and allow the private and public sectors to work together to improve educational attainment.

The best path to social and economic mobility and an improved life trajectory is through education.

In case you got bored and your attention wondered, the “Cliff Notes” are as follows:

The income disparity in our country has been growing for 40 years, and this increasing inequality is putting pressure on the social cohesion of our nation. Commitment to our country’s institutions, including colleges and universities, and values, including equal opportunity and economic and social mobility, depends on everyone feeling that these institutions and values serve their welfare and their family’s welfare. Education is America’s most effective engine for greater social equality and a real path to the American Dream. We disinvest at our peril.