



AFFORDABILITY AND DEMAND

{ FINANCIAL SUSTAINABILITY
FOR INDEPENDENT SCHOOLS }

D. Ralph Davison Jr. and Jean Davison, Editors

MANAGING VALUE: THE MARKETING PERSPECTIVE ON AFFORDABILITY AND DEMAND

By Jeffery T. Wack

The 1980s were difficult times. Home mortgage rates stood at 11 percent, doubling the cost of a house. The country was in the midst of several years of recession. The baby boomers had graduated, but their babies were only approaching school age. Black Monday, October 19, 1987, the largest drop in the stock market since 1914, shrunk endowments double-digit percentages overnight, forced the world's markets to stop trading, and was completely unexpected and never explained. As those of us around then remember, these were hard times for private schools. In 1991, NAIS published *The New Marketing Handbook for Independent Schools* — not a coincidence; it was too late for some schools, but this book had a clear message: Schools needed new kinds of management skills in order to shape their futures.

FROM SINKING TO FULL SAILS

In contrast, NAIS StatsOnline figures show that the decades since have been benign times for independent schools generally. The several key indices of school health — applications, enrollment, fund raising — have grown at roughly 2 percent per year. They have grown despite the fact that the cost of attending an independent school has grown even faster! Many industries would be envious: Raise prices yet sell more? To what should we credit being so in demand?

Marketing professionals understand demand as reflecting a dynamic balance between the state of the marketplace and what the seller is offering. On the one side are factors completely out of the control of the seller that will increase or decrease the demand, irrespective of what the seller does. On the other hand, the seller can control what for the moment I'll inelegantly refer to as its "of-

fer." Indeed, in a market economy, one should expect that the marketplace will change, and thus it is a major responsibility of leadership to manage demand by adapting what it is offering to that marketplace — that is, if one wants to remain in operation.

UNCONTROLLABLE MARKET FORCES

In the case of private schools, five categories of marketplace forces, in combination, are key drivers of market demand.

GOVERNMENT POLICY

Unacceptable public schools increase demand for private schools, and poll after poll has tracked the public's eroding confidence in the public school experience. In a survey in 1975, 58 percent of the respondents expressed confidence in public schools, but this percentage had declined to 36 percent by 1999. Eight years later, with No Child Left Behind legislation into its implementation, tracking studies conducted by the Educational Testing Service found that parents' grades of "my child's public school" are unchanged since the baseline year of 2001, a GPA of 2.8, a gracious B-.¹

Every admissions director has heard the litany of dissatisfiers that have led applicants to their door: Parents complain that public school class sizes are too large to allow the attention their child needs; safety is an issue, including the presence (or the threat of the presence) of drugs and alcohol; the curriculum is not challenging; kids get lost in the system; parents are not kept informed; teachers teach to the tests; and so on. Each of these is a cue to what parents value and what drives their interest in independent schools.

Because state and local governments have a greater impact on schools than federal policy, the acceptability of public schools, and thus the extent to which dissatisfaction with them drives demand for private options, varies widely across the country. In an area of rapid growth in south Florida, a mother in a focus group told us that as a result of new schools opening and annual redistricting, her seventh-grade son had already attended four different schools — without the family having moved! San Franciscans are experiencing unsettling rounds of public school closings. In my state (Connecticut) as in many others, the low bond rates of the past few years fueled a school building boom; as these public schools have come online, their operating costs are proving higher, so programs and staffing are suffering. Yet some public schools — typically in districts with extraordinary tax bases, places with names like Greenwich and Winnetka — seem to have unlimited resources and parent support.

In short, much as we would like to believe that all those people submitting

¹The most recent "Americans Speak" poll (2007) is located at <http://ets.org>. Select "No Child Left Behind" from Education Topics.

applications to our schools are diehard independent school fans, the reality is that a large proportion of them would be more accurately characterized as public school refugees. In that way, demand is affected by government education policy. Will the future see better or worse schools in your market?

DEMOGRAPHICS

A market's demographics are relevant to demand in two ways: quantity and quality.

In the wake of the independent school closings of the late 1980s came wonderful news: The number of children born was on an upward trend, and in 1990 the Boomers had a record number of babies, a number not surpassed in the 17 years since. This upward trend — averaging about 1.5 percent more students per year — fueled demand for all things related to children for almost 20 years. However, from every peak the only direction is down. Those born in 1990 are mainly 2007's high school seniors. Classes following them, and for the foreseeable future, are slightly smaller in number.

These are the national trends, however, and demand is local. School people in states like Arizona and California and Maine and Pennsylvania may be saying to themselves, "That's not what's happening here," and they may be right. As is well-documented elsewhere, the K-8 enrollment in warm-weather states continues to track upward, demand is strong, and new private schools are opening; but enrollment in cold-weather states is slowly declining, accounting in part for fewer applications. Similarly, schools in the ex-urbs of metropolitan areas tend to be finding more students in their markets, while those schools in the centers of major cities tend to experience declining numbers of students from the geographical area they've historically served.

Absolute numbers often hide the qualitative stories that are also relevant to demand. Perhaps the most significant story in the numbers is the changing color of these students, attributable to high rates of immigration from non-European countries and to differential birthrates among the races. For example, in the Northeast of 1972, 81 percent of K-12 enrollment was white; in 2003 it was 65 percent. Most of this shift is attributable to the increase in the number of Latinos, the percentage having at least doubled in every region of the country since the 1970s. In the West of 1972, 15 percent of students were Latino; in 2003 the number was 36 percent.

For a sense of how dramatically a school's market can change, consider Montgomery County, Maryland, the primary market of independent schools like Landon and Holton-Arms. The Montgomery County public school system of the early 1970s was more than 90 percent white; today it is 41 percent white, 23 percent African American, 21 percent Latino, and 15 percent Asian-American.²

² Montgomery County Public Schools, online at <http://www.montgomeryschoolsmd.org/about/>.

The relevant point about the quantity and qualities of demographics, of which the shift in the racial makeup of the market is but one example, is this: If different ethnic groups in the market differ in the degree to which they are inclined to enroll at an independent school, then shifting percentages among these groups will also alter demand for an independent school education. If, as is the case in most markets, the number of students in total remains constant as forecasted, yet there is a decline in the share of these students who are white, the math says that there will be fewer white students. Schools that depend on enrolling only white families will likely see applications trending downward.

SOCIAL FORCES

It is useful here to share the marketer's distinction between primary and secondary demand in order to explain the focus on parents. Primary demand in this context would mean demand for independent schooling in general, whereas secondary demand means the choice among independent schools. Proprietary research conducted by JTWack & Company LLC routinely shows that primary demand is overwhelmingly determined by the parents — that is, they decide whether or not their child will attend an independent school. These days, secondary demand, the choice of which school, is overwhelmingly driven by the student, especially when the choice is a high school. Therefore, because our topic is demand for independent schools generically, my focus is on parents.

The reality of today's parents, and to a lesser extent of today's students, is another factor outside a school's control that is driving demand for independent schools. Rather than cataloging these realities, I'll offer a few relevant themes as examples.³

Parents fear for their children's futures. And the more they worry, the more motivated they are to do whatever they believe will enhance that future, including paying tuition for elementary and secondary schools. What are they afraid of? The list is long, but here are a few of their fears:

Compared with that of their own parents, the workplace of today is a more turbulent place (a land, I submit, completely unfamiliar to most of those in independent schools). Performance evaluations and an emphasis on improvement are constants and largely determine salaries and bonuses. Yet divisions are sold, companies "re-org," positions are lost, and even if by the grace of God parents themselves dodge the proverbial bullet, they see other competent colleagues and friends suddenly looking for jobs. At such times, the value of a strong resume and good connections is brought home — and affects decisions about their children.

Perhaps the most obvious example of this is college admissions, a situation that induces a degree of anxiety among many parents that verges on the ridicu-

³ For a more comprehensive presentation on this topic, see "Everything You Always Wanted To Know about Independent School Parents" by Michelle Gall, *Independent School* magazine, Summer 2006.

lous. However, at a time when elite colleges reject nine out of 10 applicants, this anxiety is not entirely unjustified. The Ivy League hasn't added undergraduate capacity in a generation (some may do this; Yale is publicly discussing building a pair of colleges in order to increase enrollment 12 to 15 percent). And many colleges are seeing double the number of applications they did 10 years ago, reflecting the multiplicative impact of a 30+ percent increase in the number of prospective students (as reflected by the increase in SAT-takers). Moreover, according to UCLA's Higher Education Research Institute's *The American Freshman* surveys, each of these students is submitting 30 percent more applications than did each college freshman in 1997.⁴

In this economy, there is nothing quite like the combination of scarcity and fear to fuel demand. Colleges' widespread adoption of the common application several years ago has also made applying to more colleges easier.

One also often hears the views of "the consumerist" parent lamented, or discounted, by teachers or administrators. There are, of course, many bad behaviors connoted by this term. On the other hand, today's typical independent school parent is without question a more sophisticated buyer of education than were parents of the previous generation. For example, many independent school parents were themselves solid students (perhaps they even attended your school, where you taught them to question, think creatively, and be proactive!); they were admitted to good colleges and maybe even spent years in graduate training. Indeed, given the profile of faculty of many schools, the parent body is often older and better educated than are the teachers. It wasn't always this way. But if buyers who are better educated (call them "consumerist" if you must) are also buyers who are more discerning, independent schools of quality win, so let the trend continue.

In sum, many social forces and attitudes also contribute to the likelihood that parents will seek private educations for their children.

COMPETITION

The extent to which a market offers acceptable alternatives to what would otherwise be "our" customers is also a determinant of demand. Harkening back to the 1980s, the choices for parents in most markets were relatively finite. They consisted of one's neighborhood public school and perhaps the parochial or even the independent school. The nature of competition today is different; the nature of competition tomorrow will be different again.

The most obvious change is in the variety of alternatives available. For starters, while the public systems of the past offered almost nothing in the way of choices, about one in six children now have a choice of publicly funded options,

⁴ *The American Freshman, Forty-Year Trends: 1966-2006*, online at www.gseis.ucla.edu/heri/PDFs/pubs/briefs/40yrTrendsResearchBrief.pdf.

magnet and charter schools being chief among them.

In the private school arena, the nature of competition varies depending on the area. In some metropolitan areas, the Catholic diocese has closed schools, reducing the number of students attending parochial schools. In contrast, the Tucson, Arizona, diocese has added three high schools in the past five years. In fact, the growth of religious schooling options is the more dominant theme in most of the country.

Finally, the National Home Education Research Institute reports that the number of children home-schooled almost doubled, from 1.3 to 2.4 million, from 1998 to 2004. I've taught several of these students at Yale — they would have been great kids for our schools.

Each of these alternatives appeals to a particular slice of the education market. Whether their effects on enrollment for any particular independent school are marginal or major depends on the circumstances of the local market.

I would add two other ways in which competition affects demand for independent schools:

Colleges compete for the dollars that would otherwise be available for pre-college education, a factor made more explicit by the advent of federal tax-advantaged accounts designed to incentivize saving for college (i.e., 529 plans). As a reality check, try plugging the relevant numbers into a college savings planning calculator, as many young parents already have. Fidelity Investments' College Planner (available online at www.fidelity.com) says that parents with a first grader this year for whom they expect to pay four years of tuition and room and board at the average private college should be saving almost \$18,000 each year for the next 11 years. Forced to choose, and more will be, most parents will opt to ensure that their children can afford college.

Second, the growth in non-tuition revenue (call it donations) that schools have been able to attract from parents, alumni, and even grandparents has truly been impressive. However, many of the development experts I talk with are concerned that the rate of increase in giving is not sustainable. They worry that in asking for the large campaign contribution today, they are draining those dollars they would have collected when the donor is asked later. In effect, the school's present ask is competing with its future ask. In addition, fund raising has been a growth industry like almost no other. The number of federally registered non-profits in education has more than doubled since 1995 (this excludes colleges),⁵ and nearly all of them fund raise. Many, many other institutions are seeking your alumni's dollars.

HOUSEHOLD ECONOMICS

Other chapters in this book address the topic of income. I would underscore

⁵ National Center for Charitable Statistics online data center at <http://nccsdataweb.urban.org/>.

that from a marketing professional's perspective, family income is but one more uncontrollable factor driving independent school demand. The standard line is that independent schools are less affordable, mainly because of multiple years of inflation+ increases in tuition. Indeed, median tuition as a percentage of median family income has grown considerably, with median ninth-grade tuition representing 24.9 percent of median family income in 1990 and representing just over 30 percent (30.7 percent) in 2006.⁶ For the 2007–08 academic year, a family of four would need about \$128,000 to be able to pay the ninth-grade median tuition of \$19,100, using the SSS formula. Given that only about 12 to 14 percent of families earn that much,⁷ financial aid and other forms of tuition discounting are indeed necessary in order to encourage applications from the vast majority of lower-, middle-, and even most upper-income families. Presumably, the more discounting, the better / for them.

On the other hand, Federal Reserve income data suggest that for the vast majority of families who populate our schools, namely full-pay families, independent schools have become *more* affordable. This is because while income growth for the middle and lower classes has barely kept ahead of inflation, income and wealth at the high end have exploded. The average high school tuition as a percentage of average income among the top decile of U.S. families was 8 percent in 1995; despite a 60 percent increase in average tuition, it was only 9 percent 10 years later. In 2007, for those families earning roughly \$250,000 or more, the rate of income growth has far exceeded on even a percentage, much less an absolute, basis the increases in tuition. Moreover, according to the Federal Reserve's triennial Survey of Consumer Finance (last done in 2004), the number of \$1 million+ net worth households has more than tripled since 1995.

In short, if one focuses on the middle- and lower-income families, tuition increases without concomitant increases in financial aid must be dampening demand. If one focuses only on the segment that has long been attracted to independent schooling, the highest income families, it is likely that most see independent schools as more, not less, affordable. However, again we need to be cognizant of the fact that the family income trends cited are national; each school must deal with its local demographics.

In summary, all schools are subject to strong market forces, forces over which they have no control. In some places and some times, the weight of these forces so strongly favors independent schools that the enrollment picture at even schools of poorer quality looks healthy. However, the opposite is also observed: At different places or times, market forces can conspire to put even the best managed schools in hopeless situations.

⁶ Based on family income data from the U.S. Census Bureau, "Historical Income Tables — Families," and on tuition data from NAIS Statistics, National Tables.

⁷ Estimate based on U.S. Census Bureau data, "Table FINC-07. Income Distribution to \$250,000 or More for Families: 2006."

THE CASE FOR FOCUSING ON VALUE

Early in this chapter a distinction was made between market factors that drive demand but are outside the control of the seller and factors influencing demand that are in the control of the seller. In combination these factors define the purview of marketing. Marketing is the management function the primary purpose of which is to manage demand. This is done by adjusting the seller's "offer" in accordance with the forces in the marketplace. Thus, demand is a combination of both external market factors and how we adapt our marketing (see Figure 1).

Economist types and marketing types don't always see eye-to-eye on what drives consumers' choices. Do a survey of the non-purchasers of most any product or service, including private schooling, and be assured that the most frequent reason that will be given for not buying is "the price." Economists may believe this, but seasoned marketing professionals won't. Indeed, we marketing types will contend that by focusing on price — in the independent school world, we use the euphemism "affordability" — one mis-defines by half the factors determining demand.

Marketers define the challenge of managing demand in terms of managing value. The marketer's task is to devise marketing activities and integrate marketing programs to create, communicate, and deliver value to buyers. Unfortunately, the term "value" is as misused in casual conversation as the term "marketing." But to the marketing professional, there are few terms we want to be more precise about than value. The following simple model shows why marketers are adamant about the need to shift the focus of discussion about independent school demand from "affordability," and the strict economist notion that price determines demand, to "value."

$$\text{VALUE} = \text{BENEFITS} / \text{PRICE}$$

Buyers make purchase decisions based on perceived value. The denominator of the value equation is price. However, a purchase decision is also determined by what one anticipates getting as a result of a purchase, short-handed in the numer-

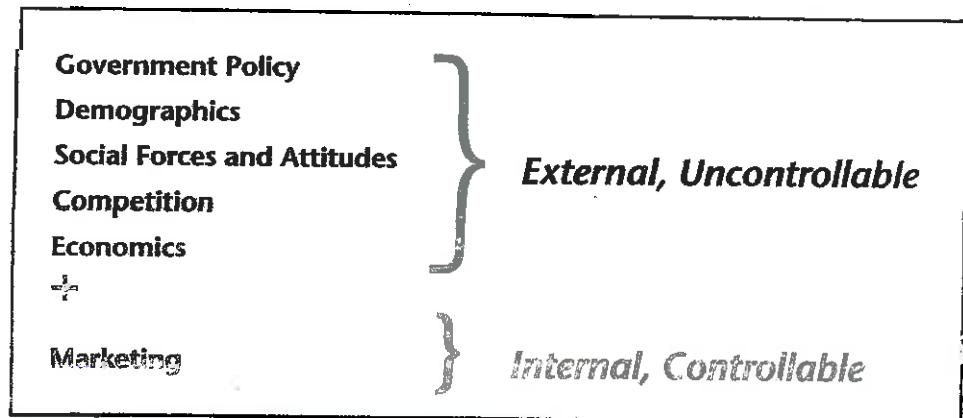


FIGURE 1: KEY FACTORS OF MANAGING DEMAND

ator of the equation as “benefits.” Parents make their decisions about whether to have their child attend an independent school not on the basis of the cost alone but on their assessment as to whether they are maximizing value. The more value they anticipate, the more likely they are to buy.

According to this equation, there are two ways to alter value. Let’s take them in turn.

One is to change the denominator, price. Lower your tuition or offer a scholarship or grant, and the B:P ratio (that is, value) increases, along with decisions to purchase. Yes, the school is made more affordable, and demand increases.

The other half of the value equation is the numerator, namely benefits — features of the school such as facilities, course offerings, and class sizes are examples of benefits. The value equation is also increased, and the price held constant. To the extent that buyers believe they are receiving more or better benefits, this results in a greater likelihood of purchase and more demand.

Marketing’s position is that even if a school does not lower its price, it can increase value, and thus demand, by focusing on boosting the numerator. Indeed, tuition discounting would be the last of the tricks that a marketing pro wants to employ — it is too easy! Conversely, as any school that has attempted a monster tuition increase in a single year has learned, a school can erode its value if it increases its price faster than it increases its perceived benefits.

MARKETING = MANAGING DEMAND

Another difference in the marketer’s worldview is that we look at the product or service through the customers’ eyes as much as we do through the sellers’ eyes. This approach makes us a real pain to those heads and deans who think that demand is simply a matter of relentless focus on building a better quality mouse-trap — er-r-r, program — and that only they, the sellers, are the judges of what is better. Marketers must argue the view that the decision to buy or not is also based on the buyer’s assessment of value. Therefore, in order to manage value, we need to understand customers and their perceptions of both the numerator (what the customers believe they are getting) and the denominator (what they perceive they are paying). The emphasis on the customer perspective is why consumer and market research is so essential to data-driven decisions. As I caution the administrators who attend my Marketing and Advancement Institute, without good information about the market, managers guess rather than manage.

Marketing consists of numerous decisions on value-enhancing marketing activities. The traditional depiction of marketing activities is in terms of the marketing mix, or what I referred to earlier as the “offer” to the marketplace. Basically, the marketing mix is the set of tools the organization has at hand to pursue its marketing objectives, tools everyone who has ever taken a marketing course will fondly remember as “the 4 Ps” of marketing: Price, Product/Service, Place, and Promotion. A sample of the marketing variables that would apply to indepen-



FIGURE 2: SAMPLE OF MARKETING TOOLS COMPOSING THE MARKETING MIX

dent schools is shown under each P in Figure 2.

Simply put, an organization can't change the market forces it can't control, but it can alter demand by improving (or worsening) its offer to this market. The Ps are the categories of tools to do so.

PRICE

If you change tuition, demand shifts in predictable ways. However, buyers assess price less in absolute terms than in relative. What are other schools charging? What is the risk that tuition will escalate rapidly, so rapidly that I'll suffer the embarrassment of having to withdraw my child before he or she graduates?

In independent schools we don't do ourselves, or prospective families, any favors by making "price" so difficult to find out. How many of the 90-plus percent of families with less than a couple hundred thousand dollar incomes are willing to go through the following in order to learn, at the very end, what they will be expected to pay to have their child attend a school?

- Invest hours of time completing paperwork and applications
- Visit open houses, and take tours
- Subject their child to admissions tests
- Risk the possible repercussions of asking teachers to write recommendations and signaling the possibility of the child's leaving his or her present school
- Reveal sensitive financial and family information
- Spend several months wondering and worrying while the admissions and financial aid decisions are deliberated

Most schools have vastly more inquiries than applicants. One suspects that a

large share of inquiries opt not to apply because they weren't willing to invest the energy and time schools require in order to answer a fundamental question so readily available for virtually every other product and service in this economy: What will it cost?

PRODUCT/SERVICE

Improve or worsen the benefits one delivers, as viewed by the customer, and demand shifts accordingly. In 2007, NAIS completed a public opinion poll my firm first did in 1999 that is designed to track perceptions of independent schools and what factors define a quality school. Figure 3 shows that the top three benefits families expect in a quality school are safety, excellent teachers, and "a climate that says it's okay to study and excel." A school the market believes is delivering these benefits better than any other school will be in highest demand. You should review the NAIS survey at www.nais.org, Resources and Statistics, Advocacy Initiative, to learn the relative importance of a variety of factors to parents' definitions of an excellent school.

PLACE

The relevance of the concept of Place (or Distribution) is more obvious for the sellers of goods than for the sellers of services. However, in the school context,

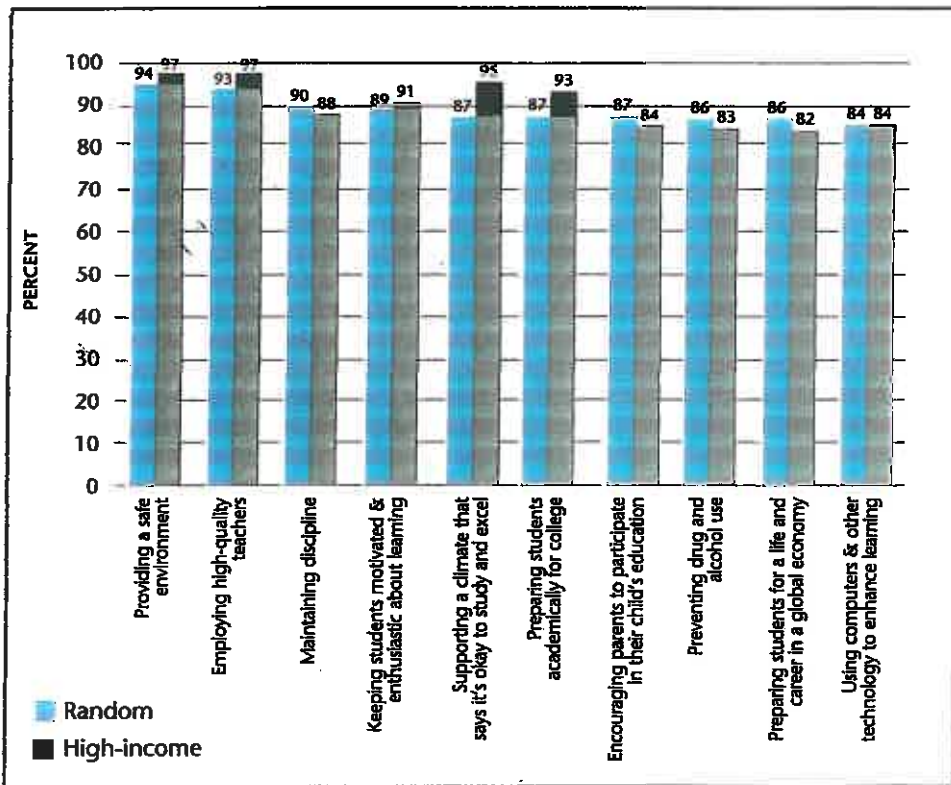


FIGURE 3: TOP 10 CHARACTERISTICS OF A QUALITY EDUCATION

Source: National Public Opinion Poll—Awareness and Perception of Independent Schools, 2007, NAIS, p. 5.

this concern can be envisioned to include such elements as facilities, accessibility (e.g., location, school calendar), and policies and procedures that shape admissions and fund raising. Build top-notch facilities, level barriers in the admissions process, provide bus services to new markets, and applications go up; offer alumni events in new cities and online giving, and donations go up.

PROMOTION

Communicate passively or thoughtlessly to the marketplace, and potential customers will know neither who you are nor why you are relevant to them. However, the more common problem in many independent schools these days is thinking that — and spending as if — communications is the only, or the most effective, tool at the school's disposal by which to alter demand.

Finally, the marketing concept says that one can more effectively manage demand if the use of these tools is integrated and aligned with market objectives. Two key themes of integrated marketing are that (a) many different activities convey value and thus managing these touchpoints is critical; and (b) marketing activities should be coordinated to maximize their joint effects.

CONCLUSION

In focusing on affordability's effect on demand, one risks overemphasizing pricing and not responding to the fact that cost is only one among many factors that determine demand for independent schooling. Many marketplace forces are outside the control of any school but are, nevertheless, important to understand in order to guide institutional planning. At the same time, in all but the most hopeless markets, schools can apply the management discipline of marketing to enhance demand by focusing on value; only if that doesn't work would a marketing professional consider price discounting.

Jeffery T. Wack is President of JTWack & Company LLC in North Haven, Connecticut, and currently serves as a trustee of NAIS. Jeff has participated in several NAIS workshops.