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## **Fitch: Higher Education Tuition Hikes Insufficient to Offset Inflation Pressures**

Fitch Ratings-Chicago/New York-14 July 2022: Inflation's effects will weigh on college and university budgets over the next few years, Fitch Ratings says. Inflationary pressures are reflected in tuition increases, lower capital outlays, less debt issuance and reduced endowment spending power, which will have longer term repercussions for operations and could also negatively affect enrollment. Schools will need to continue managing expenses or supplement revenues to preserve their budgetary flexibility.

Fitch forecasts average annual inflation of 7.8% and 3.7% for 2022 and 2023, respectively. Higher education wages increased in 1Q22 by around 3% yoy, slightly lower than broader wage trends amid a tight labor market. Increased wages are difficult to lower once in place and will have a significant impact on operating budgets, with personnel costs comprising an average of about 30% of a college's expense base.

Tuition has increased over 5% per year since 1980, with the exception of 2020-2021 and 2021-2022, when tuition was held flat. Fitch expects larger tuition hikes as universities try to keep pace with higher costs and continue to recover from foregone revenues and other pandemic impacts. We expect net tuition growth will remain constrained at best, with more challenged institutions facing declines.

Tuition price increases may dampen student demand at a time when the value proposition for a degree remains under scrutiny. Recent tuition rate increases at more competitive universities have been as high as 6%, but importantly, are at least partially offset by institutional aid at schools with available internal resources. Private institutions with stronger demand characteristics inherently retain more pricing power, while some less selective institutions that are typically much more reliant on student fee revenue will need to make sharper adjustments to their expense base to counter revenue pressures. Lower enrollment is a risk if some students delay or forgo entry into higher education, given the prospects of a strong labor market and rising cost of living.

Public universities have benefited from favorable state budgetary conditions, which have supported growth in state funding for higher education. However, state funding, which comprises about 24% of total public university revenue, may not be sufficient to fully compensate for rising operating costs. In addition, public universities' pension liabilities and required contributions may increase as a result of COLA adjustments, and may not be offset by corresponding increases in state funding. While tuition increases at public universities may be necessary to preserve budgetary balance, such increases are often tempered by caps, state approval, and their public mission to keep higher education accessible and affordable.

For both public and private schools, federal aid has acted as a meaningful replacement for lost revenue and helped preserve margins and budgetary flexibility in both fiscals 2021 and 2022. That aid has now largely been used, and institutions with underlying structural imbalances may see widening budget gaps in fiscal 2023 and beyond due to expense pressures. Cost cutting may be the

only option for those institutions lacking financial flexibility or accretive revenue diversity. Colleges and universities are likely to curtail capital plans when under financial pressure, as some schools have done throughout the pandemic, particularly as construction and financing costs increase. While endowments enjoyed a very strong 2021, market performance has been choppy in 2022 and inflation may constrain endowments' effective spending power.

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The above article originally appeared as a post on the Fitch Wire credit market commentary page. The original article can be accessed at [www.fitchratings.com](http://www.fitchratings.com). All opinions expressed are those of Fitch Ratings.