CHAPTER ONE

Introduction

> This process of Creative Destruction is the essential fact about capitalism. It is what capitalism consists in and what every capitalist concern has got to live in . . .
>
> —Joseph Schumpeter, *Capitalism, Socialism and Democracy*

One thing is certain: when Enron Corporation collapsed in 2001, no one doubted that there was a problem. Once the fraud and manipulation that underpinned Enron's arcane business strategies came to light, the evidence of impending failure came swiftly. The company's stock price—the ultimate measure of value in a free market economy—plummeted, and in the wake of that sudden decline the company's bankers and creditors ran for the exits. Lines of credit were closed down, liquidity disappeared, and bankruptcy ensued.

The repercussions of the Enron collapse were widespread. Workers lost their pensions, senior executives went to prison, and Congress enacted the Sarbanes-Oxley Act to tighten management and board accountability. In the corporate marketplace, the metrics of success and failure are known, and the rise of new companies—and the decline and disappearance of others—is the rule rather than the exception. As the buggy whip gave way to the Model T, as Studebaker gave way to Honda, as Royal gave way to IBM, now Microsoft looks to see if Google or some yet unseen threat will be its death knell.

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But even as empires rise and fall, and Schumpeter's process of creative destruction rolls onward,[1] the great institutions of higher education have continued, as if immune to the pressures of change. Oxford and Cambridge witnessed the rise and fall of the Empire and continue to reign among the world's great universities, even as the last of England's great industrial companies are being sold off to foreign buyers. America's higher education system remains the enduring jewel in the crown of the world's dominant economy, and great private universities such as Yale, Brown, Duke, Stanford, Carnegie-Mellon, and Vanderbilt have become enduring global brands, long after the men who founded them and the companies they built have faded from view.

Over the past quarter-century, however, competitive pressures have increasingly affected the world of higher education. Beginning in 1975 with the publication of its report *More Than Just Survival*,[2] the Carnegie Foundation warned of the looming impact of demographic changes and declines in student enrollments on the survival of colleges and universities. Eight years later, George Keller opened his book *Academic Strategy* with a daunting statement: "A specter is haunting higher education: the specter of decline and bankruptcy. Experts predict that between 10 percent and 30 percent of America's colleges and universities will close their doors or merge with other institutions by 1995."[3]

Needless to say, 1995 passed and no wave of bankruptcies had taken place. Nonetheless, the nature of the higher education marketplace has changed. The rankings provided by *U.S. News and World Report* have become the most recognized measure of institutional performance and quality, and higher education is increasingly seen by the American public as a private good rather than a public good.[4] However, while few question any longer that higher education is a business, it remains difficult to point to widely accepted metrics of success and failure against which to measure institutional performance. In 2006, the federal Commission on the Future of Higher Education emphasized this state of affairs, as it lamented the lack of data on student learning, institutional effectiveness, or operational productivity.[5]

Against this backdrop, the story of the decline of Drexel University in the 1980s and into the 1990s provides a case study of what the future holds for colleges and universities should they fail to embrace the implications of competitive markets on their world. Unlike the collapse of Enron, which happened with stunning speed, Drexel's decline was drawn out over many years. In the higher education world, market

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feedback and the related impact on revenues takes years to play out. For trustees, it can be difficult to recognize long-term trends and other signals that herald problems on the horizon, and—as was the case for the trustees of Drexel University—it can be easy to miss the fact that the water temperature around them is rising.

In 1984, Drexel admitted the largest freshman class in its history. Buoyed by the national recognition that it had received two years earlier as the first university in the country to require that all students have a personal computer, the school founded by Anthony Drexel a century earlier was by all measures as strong as it had ever been. In May of that year, long-time president William Walsh Hagerty announced his resignation after leading the institution for twenty-one years.

In the years following Hagerty's departure, the water temperature steadily rose, and within a decade of that high-water mark, the school was teetering. During those years, two presidents led the institution. The first, Hagerty's successor William Gaither, grasped the competitive threats facing the school and crafted a plan to steer the university toward safer waters. But in doing so, Gaither alienated the faculty and academic leadership, and sewed the seeds of his own downfall. His tenure was brief—barely three years—and culminated in a consuming sexual harassment scandal that was the means of his undoing by an alienated and resentful academic community. The second, Richard Breslin, was hired by the board of trustees in large part to ameliorate the stain of the Gaither scandal. Breslin responded to the charge of the board, and created institutions for shared governance and participation. But in the meantime, Gaither's plans for addressing Drexel's weakening competitive position were set aside, and the school's fortunes deteriorated further.

As the Drexel story illustrates, failure in higher educational institutions takes time. They cannot fail in the same way and with the same trajectory as for-profit companies. Unlike in the case of Enron, shareholders cannot exit, stakeholders are bound to a longer-term vision, and the community of alumni and other civic participants who are invested in the survival of the institution work to forestall dissolution.[6] The assets of the institution are difficult to move, employees, faculty, and alumni feel a sense of themselves and their identity bound to the continued existence, and even success, of the institution, and the local community is highly invested in its permanence. In the language of the business world, universities have deep brand equity that enables them to survive through hard times and periods of mismanagement.

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Along with these attributes that attenuate the pace of failure, the nature of consumer choice further insulates higher educational institutions from rapid decline. Students enter an institution based on its reputation in the marketplace, among other factors, and intend to continue for four or five years until graduation. This cycle of consumer choice and expenditure has several implications. First, the decision to attend an institution results from the reputation and perception of value that has been built up over a period of years, and while the amount of information available to the student-consumer has increased dramatically with the growth of the Internet, reputation and prestige remain long-lived assets that change slowly. Second, a given freshman class will cycle through an institution over a five or six-year period. As such, declines in freshmen applications and enrollments take years to fully impact an institution, and so it was at Drexel.

Drexel's slide continued for the better part of a decade. By 1995, after years of scandal, layoffs, and a bitter strike, the university's financial reserves had been fully expended, applications had plummeted, SAT scores of incoming students were steadily declining, and the enrolled freshman class was just over half of the size of the class that had entered in Hagerty's last year. Members of the board of trustees feared for the ability of the university to survive, and in informal strategy sessions discussed the possible sale of Drexel to the University of Pennsylvania, its neighbor in West Philadelphia.

Ultimately, the board dismissed Breslin and hired Taki Papadakis as his successor. Papadakis implemented a turnaround plan that mirrored many of the attributes of Gaither's plan from a decade earlier, and that sought to rebuild Drexel's historic brand around technology, cooperative education, and its urban location.

Seven years later, the board announced the acquisition of MCP Hahnemann Medical College, and the creation of the Drexel University College of Medicine. With that acquisition, less than a decade after the nadir of the financial crisis that gripped the university, Drexel's fortunes had reversed. Over the six-year period beginning in 1995, university revenues grew eighty-one percent, externally funded research expenditures grew fivefold, freshman applications tripled, full-time enrollment doubled, and incoming student SAT scores had rebounded to historic levels.[7]

Notwithstanding the attributes that set universities apart from their corporate counterparts, the Drexel experience suggests that there is one prerequisite for a successful higher education turnaround that mirrors the corporate experience. In both worlds, success depends first

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on the quality of the diagnosis of the problem and development of a plan in response to that diagnosis. In the corporate universe, the linkage between the cause of the decline and the strategy for recovery is taken as gospel. If the problem stems from a market or strategy problem, the turnaround plan must focus on strategy. If the source of the failure was related to internal operational problems, the plan must focus on that. Simply stated, you have to fix what is broken.[8]

This logical construct that leads from the diagnosis of the problem to the strategy for recovery is not an article of faith in the world of higher education. For institutions facing decline, retrenchment and cost-cutting strategies are often the first tack taken in the face of revenue and enrollment downturns and worsening market conditions, for the simple reason that it often appears to be easier to cut the budget than to garner the political support across the institutions necessary to affect fundamental changes in the mission or other essential features of an institution which may have lost salience in the marketplace.[9]

The Drexel story suggests that this conventional wisdom may be misguided. As Taki Papadakis observed upon arriving at Drexel at its nadir, as a high fixed-cost business, a university facing declining enrollment cannot cut its way to solvency, as the result is higher per student costs. As in the corporate world, a decline resulting from shifting markets and failures of strategy must be fixed by addressing the cause of the problem. In Drexel's case, after years of cutting costs, the solution ultimately entailed implementing a market strategy that enabled it to increase both enrollment and price.

The Drexel experience illustrates the risks to higher educational institutions in the competitive marketplace, and the challenges to trustees entrusted with their guidance. Higher educational institutions do not move quickly, as defining institutional attributes such as shared governance and academic tenure mitigate against rapid responses to changes in the competitive landscape, and they do not quickly learn from their competitors' mistakes. The Drexel experience came on the heels of financial crises at New York University in the 1970s and Northeastern University in the 1980s, similar schools that historically served working-class and immigrant populations, and that were buffeted by changes in the competitive landscape—most notably the expansion of lower-cost public college alternatives—that led to shifts in demand and declining enrollments.[10] However, as similar as the crises at NYU and Northeastern may have been, the lessons they might have offered to Drexel trustees went unheeded.

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The Drexel story—like those of NYU and Northeastern before it—suggests the fundamental tension that exists as nonprofit universities find themselves in increasingly competitive markets. Unlike for-profit corporations, which are driven to maximize economic opportunity and shareholder value, nonprofit corporations are intended to be mission-driven with the presumption that economic considerations are secondary. In a competitive market, however, universities must compete effectively if they are to survive to serve their mission. In the case of Drexel University, its founding social welfare mission was no longer tenable in the face of lower-cost public alternatives. Caught between the original mission and the immutable realities of the marketplace, the mission was forced to evolve.

The balancing of that tension—between the interpretation of the mission and competitive market forces—is a central challenge for trustees and administrators, and ultimately for faculty if the rhetoric of shared governance is to be born out in practice. The challenge is to chart a course that combines a mission that galvanizes the support of the wide range of constituencies across the community, and a long-term plan that is achievable within the realities of the markets in which the institution competes. Ideally, as was the case for Drexel in its commitment to cooperative education and linking education with work, the mission conveys value to the marketplace and is a source of competitive advantage. Often, however, this is not the case. For schools that have, as former Harvard University president Derek Bok suggests, "lost sight of any clear mission beyond a vague commitment to 'excellence,' "[11] competitive forces may be harsh, and all but the preeminent few may see their competitive position wane and their product increasingly viewed as a commodity.

For trustees and administrators charged with striking that balance and galvanizing the community around a plan, the path forward is difficult. In the case of Drexel, as with NYU and Northeastern, the lack of metrics that might have effectively foreshadowed looming problems undermined the ability of trustees to react sooner and more effectively. However, the larger problem was the lack of recognition by stakeholders across the institution that the university world itself had changed, and perhaps changed forever. A first step, therefore, must entail broadening community understanding that these seemingly eternal institutions have entered a new world, and are now subject to the perennial gale of destructive forces of which Schumpeter warned.

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The challenge for higher educational institutions that find themselves in increasingly competitive markets is to develop governance structures that align the interests of the constituencies within the organization. Shared governance, as that term has come to have meaning within the academy, implies a segregation of areas of responsibility between the faculty and the administration. The faculty retains the responsibility for issues of curriculum, program development and termination, and academic policy, while the administration has authority over the nonacademic and business functions necessary to the livelihood of the institution.

The problem with this model of shared governance is that the areas of responsibility are no longer clearly demarcated. Curriculum and budget are increasingly inseparable, yet a faculty committee might control one side and a provost the other. Similarly, in the modern university, academic programs, co-curricular and student life activities, international studies, internships, and advisement are increasingly interwoven and interdependent as elements of undergraduate education. In competitive markets, organizational speed and agility are increasingly important, and a governance structure that gives parties veto power rather than creating inducements to an alignment of interests will serve as a competitive disadvantage over time.

As markets become more competitive, technology evolves, and new modalities of learning become part of the educational landscape, demands for organizational adaptation and learning will require solutions that are more fundamental and less incremental. To the extent that the difficulties faced by any given institution relate to underlying market forces—and that is true in almost all circumstances—then understanding those forces and the linkages between the mission and the market is critical. Ultimately, as has been the case in the corporate world, organizational success in competitive markets will demand, and ultimately reward, new forms of organizational adaptation that go well beyond discreet strategies that impact marginal costs or revenues. Organizational flexibility, learning, and adaptation—bywords of life in the corporate world—are barely nascent characteristics of higher educational institutions, and have long-term implications for organizational culture and collective responsibility for outcomes.

At its most fundamental level, this is a story about the decline and turnaround of an American university. It is in the first instance the story of an institution whose historical mission of service to the urban working

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class lost salience in an evolving marketplace, the failure of the leadership of the institution to recognize the changes that were occurring, and the turmoil that emerged within the institution in the wake of the events that unfolded. It is in the second instance the story of an organizational turnaround, about the strategies through which the institution found its footing and recovered from a period of severe decline. However, turnarounds are as much an art as a science, and it is not the purpose of this book to provide a "how-to" workbook, or a compendium of strategies that, if diligently applied, will cure the problems of another institution.

The story that unfolds in the following chapters illustrates the difficulty of change. It is a story of decline and turnaround, but perhaps one where the story of decline holds more grist than the turnaround. This is not the norm in the literature. Fewer books focus on the decline than on the rebirth, perhaps because stories of rebirth offer hope and give us heroes. But it is in the decline, and in the struggle, where the human story lies, and where the passions run deep.

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