Angling for Applicants

A marked decline in application volume to full-time U.S. MBA programs has caused consternation among many management educators. Our concerns are evidenced by a survey of 352 graduate business programs conducted in June 2004 by the Graduate Management Admissions Council (GMAC) and the Executive MBA Council. It found that 78 percent of full-time, two-year MBA programs reported a decline in application volume between the 2002–2003 and 2003–2004 academic years.

More and more business schools are fishing for MBAs from the same applicant pool. To bring in the best catch, each school must position its boat carefully, cast a broad net, and offer more tempting bait on its hook.

by Mark Zupan

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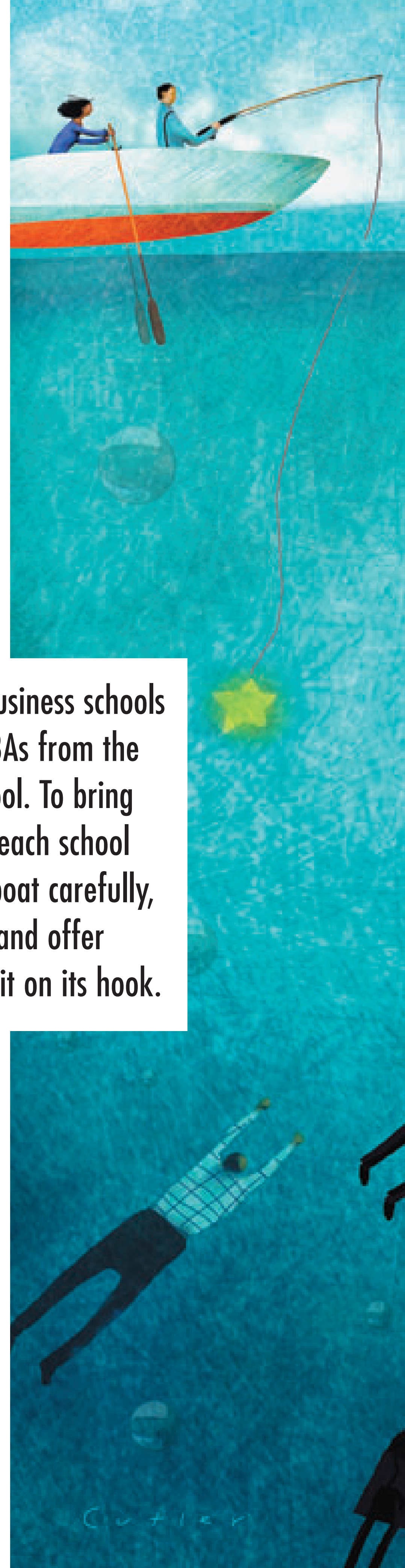

Moreover, the number of GMAT test takers fell from a peak of 228,500 in 1997 to just under 182,000 in 2004—a 20 percent decline in the number of potential MBA students. GMAT test-taking volume is down 18 percent just since 2002, indicating that most of this decline has happened in the last two years. The MBA Roundtable also estimates the decline in applications to be about 15 to 25 percent for the 2003–2004 admissions cycle.

These statistics point to a decline that compounds what has generally been a softening market for full-time MBA applications since the late 1990s. If only a few schools were seeing this decline, we might be able to localize the cause to individual campuses or regions. But the trend seems to affect business schools across the board. For instance, Kenneth Dunn, dean of Carnegie Mellon's Tepper School of Business in Pittsburgh, Pennsylvania, noted that the school's full-time applications were running 30 percent lower in 2003–2004 than in 2002–2003. The reported decline in applications in 2003–2004

ranged from 15 percent to 30 percent at prestigious institutions such as the Graduate School of Business at the University of Chicago, Darden Graduate School of Business Administration at the University of Virginia in Charlottesville, the Stern School of Business at New York University, the Olin School of Business at Washington University in St. Louis, the Kellogg Graduate School of Management at Northwestern University in Evanston, Illinois, The Wharton School at the University of Pennsylvania in Philadelphia, and the Anderson School at the University of California, Los Angeles.

In trying to explain this downward trend, many market watchers cite demand-side factors, such as changes in demographics and a decline in job placement for MBA graduates. But we must also examine supply-side factors, such as increased competition and a changing marketplace. It may be that there aren't fewer potential students; they just have more programs from which to choose. In both cases, business schools need to approach the marketplace differently and compete more effectively to make sure their most prominent program also remains their most profitable.

The Difficulty of Demand-Side Economics

For a moment, let's examine those demand-side factors, which rest largely outside of a business school's control. For example, at least part of the decrease in applications appears to stem from demographics. According to the survey conducted earlier this year by GMAC, the number of people of business school age (25 to 29 years) has declined in the United States, Asia, and Western Europe. The population of this age group declined 3 percent in Asia, from 300 million in 2000 to 291 million in 2004; 2 percent in the United States, from 19.4 to 19.1 million; and 7 percent in Western Europe, from 28 to 26 million. These declines are still fairly small, however, and they cannot account for the overall decline in demand for MBA education.

More stringent entry visa requirements, limits on H-1 B visas that allow international students to work in the United States following their MBA studies, and rising anti-American sentiment in the post-9/11 era also have contributed to declining graduate applications to U.S. schools from students in other countries. In parts of India, for example, students report having to wait 12 weeks for visa interviews, which also has contributed to the decrease. The Council of Graduate Schools reported a 28 percent decline in international applications for graduate study in the United States for this academic year. Actual international enrollments fell by 6 percent, the first decline in three decades. The most significant application decreases occurred among students from China and India, followed by students from the Mideast, Korea, and Western Europe.

The decline in international applications, despite the falling value of the dollar relative to most other currencies, may end up putting a significant dent in the $13 billion that higher education exports contribute annually to the U.S. economy. For example, the National Academy of Sciences reports that the number of people who have taken the GRE test in India and China has declined 50 percent relative to last year. Historically, this statistic has been a good predictor of international applications in U.S. graduate schools, indicating this trend may continue for the next academic year.

The economic slowdown in many other parts of the world post-9/11 has adversely affected average household wealth, and, as a consequence, applications from overseas. The William E. Simon Graduate School of Business Administration at the University of Rochester in New York, for example, has historically drawn six to 15 full-time MBA students per year from Brazil. Such enrollments have been crimped since 2000, when the Brazilian *real* lost roughly two-thirds of its value relative to the dollar.

Finally, diminished post-graduation career prospects have raised more questions about the value of investing in an MBA degree and thereby lessened prospective student interest. Between 2001 and 2004, for instance, the average starting salary and compensation for students graduating from the top 50 U.S. business schools declined by 8 percent, from $90,743 to $83,591, according to *U.S. News & World Report*. Over the same time period, the average placement rate three months after graduation fell from 96.6 to 81.4 percent at the top 50 business schools.

Supply Side: The Rest of the Story

Yes, demand-side factors have played an undeniably significant role in declining applications to full-time MBA programs. But those factors alone don't absolve business schools completely for their role in this decline. Several marked trends on the supply side have also had a hand:

A b-school boom. One of the most significant supply-side factors has been the boom in the number of new business schools entering the market to meet what was, until recently, a rise in demand for MBA education. The number of AACSB-accredited business schools has more than doubled over the

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last 35 years. Furthermore, domestic competition has grown through not-for-profit as well as for-profit suppliers. The Apollo Group, parent company of the University of Phoenix, began operations in 1976. The stock price of University of Phoenix Online has skyrocketed, as its annual revenue gains have exceeded 65 percent in each of the last three years. It now enrolls more than 200,000 students, most pursing degrees in business. This number dwarfs the enrollments of the largest not-for-profit business schools.

It stands to reason that when the number of fishing boats in the water increases, and the number of fish stays relatively constant, the average haul per boat decreases. In other words, the more business schools in the market, the more finely the customer base is divided.

Greater international competition. The overall pool of full-time MBA applications also has become more crowded because of heightened competition from schools overseas. Many overseas suppliers of full-time MBA degrees have earned AACSB accreditation over the last few decades, including the Hong Kong University of Science and Technology, the United Arab Emirates University, INCAE in Costa Rica, and the Cranfield School of Management in the United Kingdom.

Competing programs. In fact, business schools compete not only with other business schools, but also with themselves. They have added many more dimensions to management education, including EMBA, part-time, online, and accelerated one-year full-time programs, which serve as alternatives to the traditional, full-time, two-year MBA. Many schools even offer nondegree executive education.

GMAC's recent survey of graduate business schools also demonstrates that some of the decline in full-time applications may be attributable to the growth of alternative MBA program offerings. Whereas the overwhelming majority of business schools reported a sharp decline in full-time, two-year MBA applications, applications to EMBA and accelerated one-year programs appeared to be up; part-time MBA applications remained flat.

In addition, more than 500,000 Americans currently earn a degree online each year—again, many of those degrees are in business. This only further underscores the fact that we are operating in a segmented market. To continue the analogy above, the ever-growing number of fishing boats in the water is using a greater variety of nets. As a result, the average haul of fish in each of their nets is also diminished.

The rankings. One can't ignore the effects the rankings have had on business school programs. The advent of media rankings two decades ago has placed business schools under a very large lens—with full-time MBA programs receiving the most thorough attention. Under such scrutiny, business schools have had a clear incentive to raise the standards employed for full-time program admission. Their aim in doing so was to enhance their reputations. However, the more rigorous admissions standards are, the lower the number of potential full-time applicants becomes.

The rising cost of the MBA. The real price of full-time MBA education, at least at leading private schools, has roughly quadrupled over the last 35 years. This increase reflects, at least in part, the need to support the cost of research centers and rising faculty salaries. The increase also stems from greater investment in staff, technology, and bricks and mortar, fueled by the media rankings "arms race." And as the real price of full-time MBA education rises, there is a further incentive for prospective students to remain in their existing jobs, favoring enrollment in alternative degree programs instead of the full-time MBA. In many alternative programs, students not only keep earning salaries, but they also might benefit from greater tuition support. Employers are often willing to subsidize continuing education when it does not require employees to leave their jobs.

Some of the effects of these factors have been subtle. For instance, business schools have increased the average number of years of work experience required for admission to full-time programs. The norm used to be close to zero years before the arrival of rankings; the average now runs from four to seven years at leading schools. But in their efforts to show higher post-MBA starting salaries, schools have effectively pushed many potential applicants into part-time options.

In addition, as schools require more years of work experience, they inadvertently deter women from applying to full-time MBA programs, since women, especially those 25 to 40 years old, are more likely than men to juggle the conflicting demands of family and education/career. As a result, women account for less than 30 percent of the student body at leading business programs. At the same time, women represent more than 50 percent of the student body at law schools, which typically admit students straight out of undergraduate programs.

What's an Administrator to Do?

Such supply-side factors go a long way toward putting the future of full-time MBA programs in jeopardy. With competition among MBA programs reaching a fever pitch, the market may soon approximate the economist's model of perfect competition, in which the returns that can be earned in the market by a representative firm, such as a business school, are zero in the long run. Indeed, a number of deans of leading U.S. business schools have observed that their full-time MBA

programs are actually running at a deficit. They must pour resources earned by other programs into their more highly visible MBA programs, just to remain competitive.

For business school administrators, what are the implications? First, they must realize that assumptions that have carried them successfully to this point most likely will *not* carry them any farther. For instance, historically, business school administrators could safely assume greater monopoly and pricing power in their local markets for part-time and EMBA offerings. This assumption has gone by the wayside in recent years, as competition has become almost as heated locally as it is internationally.

The same is true for fund raising. At one time, a business school's fund-raising committee could assume some monopoly over its rivals, given the greater ties alumni have to their schools. That assumption is no longer safe. After all, it's unlikely that an alum, no matter what his affiliation, will want to give money to support an undifferentiated MBA program that promises zero return.

Business school administrators are likely to consider several strategies as they decide how to compete in a crowded market. Some strategies are better than others, however. There are two strategies in particular that may be the *least* fruitful for business schools to follow:

Waiting it out. Although waiting out the present decline may be the most commonly adopted strategy, it's also least likely to be effective. Demographic projections predict a healthy increase in the number of people of business school age worldwide over the next five to 10 years. For example, schools that take a "wait-and-see, do-nothing" strategy will not be competitively prepared to take advantage of any rebound in demand. More proactive suppliers in the market will already have attracted the best and brightest.

Counting on others to fail. In a crowded market, it may seem likely that other, less established schools will go under. After all, in other competitive settings, economists predict that companies that do not make a profit will fail. But counting on the failure of other providers is also not an attractive near-term strategy. First, a for-profit competitor such as the University of Phoenix has already established itself as a fixture in the market. It's not going anywhere. And second, not-for-profit business schools at most universities have historically been the cash cows providing the financial surpluses needed to underwrite the remainder of the enterprise. These surpluses are realized through overhead taxes assessed by central administrators. Therefore, as full-time MBA programs start bringing in lower or no profits, they are unlikely to be shut down. Instead, business schools will negotiate a different arrangement with their universities.

The best strategies are perhaps summarized by the title of a well-known marketing book by Steve Rivkin and Jack Trout: *Differentiate or Die.* Differentiation will be essential for full-time, two-year MBA offerings as well as for other ancillary products, such as part-time, online, EMBA, and nondegree executive education. Schools can pursue several strategies to set themselves apart quickly and definitively:

Create other sources of income. Many opportunities exist for a business school to financially support itself through its ancillary product lines. Witness what Northwestern University's Kellogg Graduate School of Management has done so effectively over the years. It has established a solid offering of nondegree executive education, including partnering with the Young Presidents Organization to develop continuing education to the membership of this well-known business group.

More recent examples include a program at Case Western Reserve University's Weatherhead School of Management in Cleveland, Ohio. It runs a program targeted to transforming successful business leaders into doctoral graduates. Other examples are EMBA programs at Duke University's Fuqua School of Business in Durham, North Carolina, and Yale University's School of Management in New Haven Connecticut. Both schools are creating specialties in the healthcare management area. Still other schools have created specialized one-year masters programs.

At Simon, we are planning to launch masters of accounting and masters of medical management programs. The former is designed to address the growing need for accounting training in the wake of Sarbanes-Oxley. The latter is intended to complement our other healthcare management offerings and appeal to the sizable population at our university's prominent medical center.

Partner up. In the coming decade, business schools will often derive advantages by creating complementary partnerships with other schools. Those schools that continue to operate solely on a stand-alone basis will most likely see their programs suffer.

For example, Columbia University's Graduate School of Business in New York has teamed with the Haas School at the University of California in Berkeley to develop nondegree offerings. Columbia also has created an international EMBA in partnership with the London Business School. A number of American business schools have found it advantageous to

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partner with institutions in emerging markets such as China, taking advantage of both growing demand and less intense supply-side competition. This was our experience at the Simon School in the late 1980s and early 1990s when we partnered with programs in Switzerland and Holland to offer an American-style MBA program to the European market.

It must be said, however, that successful partnerships take considerable time and effort. Moreover, if successful, partnerships invite competitors over time—a result that further heightens the need to differentiate one's offerings.

Develop a true identity. It's imperative for schools to examine what they have to offer. Then they must isolate—and effectively communicate—what makes them special in the marketplace. In our marketing and culture at the Simon School, we highlight several characteristics of our full-time MBA program that we feel make us different. We promote its basis in economics and analysis, its position as one of the smallest and most personalized programs in the top tier, its high percentage of students from abroad, and its specializations in technology and healthcare.

Increased competition will be a tremendous challenge to all business schools, but it's also a unique and rich opportunity. In the next decade and beyond, business schools have the chance to create new markets through differentiation and to expand the overall market for full-time MBA education. After all, a fundamental tenet of economics is that, in a dynamic setting, competition best serves the interests of consumers. Therefore, students will be better served as business schools better define their markets. In the process, the MBA will see more programmatic innovations than ever before, which will both benefit consumers of business education and reward those schools creative and disciplined enough to bring those innovations successfully to market. Z

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