

# Early Learning Opportunities and the Market: An Issue Brief for Child Care Providers in New Mexico



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*Ninety percent of children's brain growth occurs before age five. By taking advantage of this important development opportunity, children are more likely to be prepared for learning when they start school and therefore less likely to require expensive remediation.*

*Early childhood programs are a good investment because when children succeed in school, they succeed in life and don't require expensive social programs as adults.<sup>1</sup>*

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<sup>1</sup> A majority of business, community and tribal leaders in New Mexico found these statements persuasive in a recent poll conducted by Research and Polling Inc. (2010)

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# Early Learning Opportunities and the Market:

## An Issue Brief for Child Care Providers in New Mexico

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Children are influenced by their families and by all the adults in their lives. Every place and relationship affects whether and how well children are prepared for kindergarten. Many New Mexican children are in early care and education programs that can help prepare them for school. These may be called child care or Head Start or preschool, may be in a home, a center or a school. The **quality** of these programs matters – to children’s daily lives now and to their future ability to succeed in kindergarten and beyond.

### QUALITY

New Mexico was among the first states in the nation to adopt a quality rating and improvement system in 1999, now called *Look for the STARS*. All state-licensed programs have STARS, starting with 1 STAR for meeting basic regulations, going up to 5 STARS for those that are nationally accredited. By 2009, over 70% of New Mexico’s more than 1,000 licensed programs were 2-STAR or higher. As of 2011, 2-STAR signifies a program is meeting basic regulations; in just one decade, *Look for the STARS* has raised the floor of basic regulation.

New Mexico has funded New Mexico PreK since 2005. Like many other states, New Mexico Prekindergarten (NMPK) is offered in public schools and community settings. The annual evaluation reports show that NMPK is effective at improving child outcomes in both settings; children make significant gains in math, vocabulary and early literacy each year in both Public Education Department (PED) and Children Youth and Families Department (CYFD) sites.<sup>2</sup> Notably, almost 60% of NMPK in community settings (CYFD sites) is in 4-STAR or 5-STAR centers, the highest quality.

There are other clear connections between NMPK and *Look for the STARS*. Class size and teacher:student ratio (20, 1:10) in NMPK match the class size and ratio required for 4 year-olds for 4-STAR (and above). The approach to curriculum planning based on child observation with assessment of outcomes that is required in NMPK is mirrored in the STARS standards at 4-STAR and above. The pathway to these practices is laid out in the 2-STAR elements where distinct learning areas are required, and at 3-STAR where child observation and assessment guide activity planning in the distinct learning areas.

*More than 4,000 four-year-olds are enrolled in New Mexico Pre-K. More than ten times that number of children – 50,000 infants, toddlers and preschoolers – are in regulated child care in New Mexico.*

New Mexican children have access to quality programs because of these state policies and investments. More than 4,000 four-year-olds are enrolled in NMPK. More than

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<sup>2</sup> *The New Mexico PreK Evaluation: Impacts From the Fourth Year (2008-2009) of New Mexico’s State-Funded PreK Program*, (NIEER, 2010)

ten times that number of children – 50,000 infants, toddlers and preschoolers – are in regulated child care in New Mexico.<sup>3</sup> All of these young children will eventually enter kindergarten. The quality of the settings these children are in for their first five years, especially the teachers, can make all the difference in whether these children are ready to succeed in school.

## THE MARKET AND COST OF QUALITY

Several recent studies commissioned by the CYFD and conducted by the University of New Mexico offer information about the provider cost of doing business and the cost of increasing quality. The full reports contain detailed data on the specific costs involved in caring for children, by age (from infants through school-age) and by provider type; see the Bibliography.

The early care and education or ‘child care’ industry is a market influenced by the forces of supply and demand, like other service industries. Providers offer services in response to consumer (family) demand. While children are the direct recipient of services, families are the consumers, purchasing services on behalf of their children. Providers can stay in business when their cost of providing the services can be covered by the fees families are willing and able to pay.

Some cost features of child care are subject to economies of scale. A larger facility is likely to have lower per-child rent, office administration, insurance and other operating expenses. Adding more children lowers the average (i.e., per child) cost of these components. This is a common feature of many industries. ***A unique feature of the child care industry is the absence of economies of scale for the largest single expense faced by the provider: labor.*** Fixed child-to-teacher ratios mean that the lion’s share of the per-child cost of care is invariant to size of facility. For example, regardless of the size of the facility, if one teacher is required for five children, and that teacher earns \$10 per hour, the teacher-cost per child is \$2 per hour whether the child is cared for in a small family home or a large center. ***Labor costs are 70% or more of total expenses.***

## THE WORKFORCE

Teachers are both the largest cost of doing business and most important ingredient for children. Several recent studies commissioned by the CYFD and conducted by the University of New Mexico illuminate the status of the early care and education workforce. The full reports contain detailed data on the child care workforce; see the Bibliography.

***Teachers.***<sup>4</sup> The average NM child care teacher in 2010 is a 37-year-old, Hispanic female who has completed high school and some coursework beyond. She has worked 9 years in the profession, including 4 years with her current employer, and plans to stay in the field at least 3 more years. She works an average of 36 hours per week, making \$9.98/hour (about \$18,600 per year). She has access to

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<sup>3</sup> Total licensed and registered capacity is 72,654 for all ages. Assuming 75% are under age 6, the total 0-5 is 54,484.

<sup>4</sup> Over one thousand workers in regulated child care programs completed Teacher Surveys. Most worked in child care centers (867, or approximately 83%); the rest worked in homes (181, or 17%).

health insurance, but not necessarily provided by her employer. In fact, about one-third of the workforce has no health insurance at all. Of those who do have insurance, forty percent receive it through public programs such as Medicaid .

**Director qualifications.** In 2010, just over 30% of all directors (including those in charge of group or family child care homes) have a Bachelor's or Master's degree and 43% have an Associate's or higher degree. Just over 50% of all center directors have an Associate's or higher degree. Approximately half of 5-Star directors have either a Bachelor's or Masters' degree.

**Teacher qualifications.** More than half of center lead teachers have an Associate's or higher degree. Overall urban lead teachers are more likely to have an Associate's or higher degree than their rural counterparts (54% of urban teachers compared to 35% in rural areas). Happily, the actual qualifications of the workforce exceed the minimum requirements reported by programs, as illustrated in Figure 1 in the Appendix.

## SUPPLY, DEMAND AND COST

Providers have to set fees to cover their cost of doing business, and those fees must be affordable to their customers. Families are the major payer of those fees. The majority of children in child care are paid for solely by their own families (meaning fewer children statewide are receiving child care subsidies). Child care subsidy payments are related to the fees providers set and charge to families, in essence public funds pay the tuition fee (up to a limit) on behalf of children in eligible families. So, families are the primary source of revenue for the industry and their ability to pay determines the public contribution.

*Providers have to set fees to cover their cost of doing business, and those fees must be affordable to their customers.*

*The median family income in New Mexico is close to \$52,000. Full-time care for two children will take more than \$12,000 a year, or nearly a quarter of the families' gross income.*

The typical family is stretched to meet current child care prices. The median family income in New Mexico is close to \$52,000. A New Mexican family with one infant and one preschooler, both in a center full-time, will pay more than \$12,000 a year, or nearly a quarter of the families' gross income.

**Profitability.** The typical provider in New Mexico is doing better than breaking even, according to the 2010 UNM cost survey. Overall, median revenue exceeded median costs, but profitability varied by type of provider. The median revenue minus median cost (profitability) was highest among 5-Star providers, but more than half of the 5-Star providers report no rent or mortgage; median profitability measures for 2-Star providers (which are the bulk of the provider) and Santa Fe providers suggest that those categories are more likely to experience costs in excess of revenues, or net losses. See Figure 2 in Appendix for detail. It's important to keep in mind that if providers had to purchase the donated

services and materials they receive (including rent/mortgage), it's likely that their profit margin would shrink or disappear.

**Sources of Revenue.** The cost survey also collected data regarding the sources of revenue received by survey respondents. Parent-paid tuition and fees and fees paid by the state provided most of the revenue received by providers. The Child and Adult Food Program was also an important source of revenue. Very few providers had any other sources of revenue such as donations or contributions. Santa Fe providers were unusual in that 60% had received contributions or donations. Half of 5-Star providers reported receiving some contributions or donations. See the Table in the Appendix for details.

## COST AND QUALITY

So, what about quality in this market? One of the benefits of *Look for the STARS* (and all quality rating and improvement systems) is offering information to families on the relative quality of different programs. Families in New Mexico certainly do recognize and desire higher quality. The evidence is the significantly longer waitlists at higher STAR programs. Waitlists are about demand for quality. Parents often put their children on more than one waitlist, hoping for an opening in a better program. According to the recent UNM study, for all age groups, higher-star child care providers had the longest waitlists. Two urban centers, a 4-Star and a 5-Star center reported 28 full-time 1-year-olds on their waitlists. One urban 5-Star center reported an 80-child waitlist for full-time preschoolers, and one rural 5-star center reported 47 full-time preschoolers on a waitlist. Families do want quality, but do not have the resources to pay for it.

*Families in New Mexico certainly do recognize and desire higher quality. On the supply side, providers want to offer better quality.*

On the supply side, providers want to offer better quality. In the 2010 survey, close to half the providers reported they planned to seek a higher STAR level in the coming year, a clear indication of provider desire to offer better quality.

The cost of producing services increases as quality increases, according to the cost and cost of quality studies commissioned by CYFD and conducted by the UNM. Generally, reported costs increase as STAR level increases, with one exception. The facility cost for 5-Star, which is comparatively low compared to other levels, because more than half of responding 5-Star providers paid no rent or mortgage for their facilities. This is in part how higher quality programs survive.

## THE MARKET DILEMMA: COST, PRICE AND QUALITY

To stay in business providing higher quality, the provider has to charge higher fees to cover these higher costs, yet families cannot easily afford higher fees. If the fee amount begins to come close to

*To stay in business providing higher quality, the provider has to charge higher fees to cover these higher costs, yet families cannot easily afford higher fees.*

the take-home income of the parent, then families may consider other alternatives. One alternative is lower cost-care which may also be lower quality, or unregulated care which is of unknown quality. In a two-parent family, an alternative may be for one spouse to quit working and stay home with children.

If the provider cannot pass the costs of higher quality to the consumers as higher fees, then the provider may abandon the effort to offer higher quality. Alternatively, when providers cannot charge fees high enough to cover the costs, they resort to efforts to reduce their costs. One example is the lack of facility costs for 5-STAR providers discussed above. Another is buying fewer supplies and materials, common in centers and homes. Centers hold off on paying bonuses or delay staff raises. They may also reduce teacher hours, but cannot go below the regulated minimum ratios. Some providers report reducing director pay or taking no pay at all. Some of these actions, like cutting back on classroom supplies or teaching hours, may also reduce quality. Others are clearly unsustainable over time, like not paying themselves (directors). Providers' ability to increase fees is further constrained by the recession economy. For more detail on recession effects on the child care industry see the Table in the Appendix.

The bottom line is this market has fundamental problems as well as opportunities. Both providers and consumers desire higher quality (for children) yet the market alone is incapable of providing sufficient incentives for sustaining higher quality. And remember that higher quality does not only benefit the current actors in the market: everyone benefits when children are prepared to enter kindergarten and succeed in school. The basic economics of child care works against producing the quality children need to succeed in school. How can this market work better?

## **INCENTIVES FOR QUALITY**

New Mexico supports access and quality in the early care and education industry in several ways. First, the investment in child care subsidy enables low-income families to access child care, which they would be unable to do in the absence of the subsidy because their incomes are too low. The investment in NMPK enables some 4-year-olds to access a quality program with demonstrated education outcomes.

*Look for the STARS* is a systematic way to promote quality to consumers. Providers benefit from the supports aligned with STARS. For more than a decade, the CYFD has funded the Early Childhood Training and Technical Assistance Programs (TTAPs) to provide training, support and quality improvement services for child care providers and programs. On-site, phone and email help is offered as well as group training and toy/material lending libraries. TTAPs work with CYFD licensing to verify status for programs at 2-STAR and above, including conducting reliable Environment Rating Scale assessments. AIM HIGH specialists support programs to improve quality; programs serving families receiving child care assistance through CYFD have priority to participate in AIM HIGH. This focuses quality improvement resources on the most vulnerable children.

Since 2004, the CYFD along with PED and other funders has supported T.E.A.C.H. Early Childhood New Mexico to offer scholarships for tuition and books, release time from work, and bonuses or raises for



currently employed early childhood teachers who want to work on Associate, Bachelor or Graduate Degrees in early childhood education.

Finally, an essential financial support for higher quality programs is the quality differential for STAR-rated programs. This monthly amount, graduated by STAR level and paid per subsidized child, is intended to cover the additional costs of providing a higher quality program.

*Now that the highest levels of STARS incorporate key features of the practices of NMPK, the time is ripe to align these two quality systems. One quality framework can potentially reach all young children in New Mexico.*

## NEXT STEPS

New Mexicans are understandably proud of NMPK and can be equally proud of the progress made in *Look for the STARS*. Both are successful, and together can be an even stronger and more effective system. Over time, as the practice in programs has advanced beyond the lower levels of STAR standards, the minimum regulations (1-STAR requirements) have been improved. Now that the highest levels of STARS incorporate key features of the practices of NMPK, the time is ripe to align these two quality systems. One quality framework can potentially reach all young children in New Mexico.

## MAINTAIN MOMENTUM

In these times, it is essential to ***maintain current investments*** in support of the gains in quality that New Mexico has achieved. These are NMPK, STARS and the TTAPs support network, the T.E.A.C.H. scholarships and the quality differentials. Together, these are significant supports for current operation that are the down payment on future success of young children.

## GENERATE ECONOMIES OF SCALE

Another way to acquire resources to support higher quality in the industry is to find ways to generate economies of scale for some of the costs of doing business. This is happening in several states under the banner of 'Shared Service Alliances.'<sup>5</sup> Typically, a community-based partnership comprised of centers and family child care homes works together to share costs and deliver services in a more streamlined and efficient way. By participating in a Shared Service Alliance, early care and education businesses become stronger, more accountable, more financially sound and efficient, and better equipped to offer affordable, high-quality services for children and their families. The Alliances achieve cost-savings by negotiating better prices on supplies and materials, sharing administrative staff and even directors. Exploration of this concept in New Mexico is a low-cost activity with potentially significant cost-saving potential and might well be attractive to private funders.

Ultimately, both public and private investment in services for New Mexico's children is worthwhile because the school readiness of children benefits the state economy as a whole.

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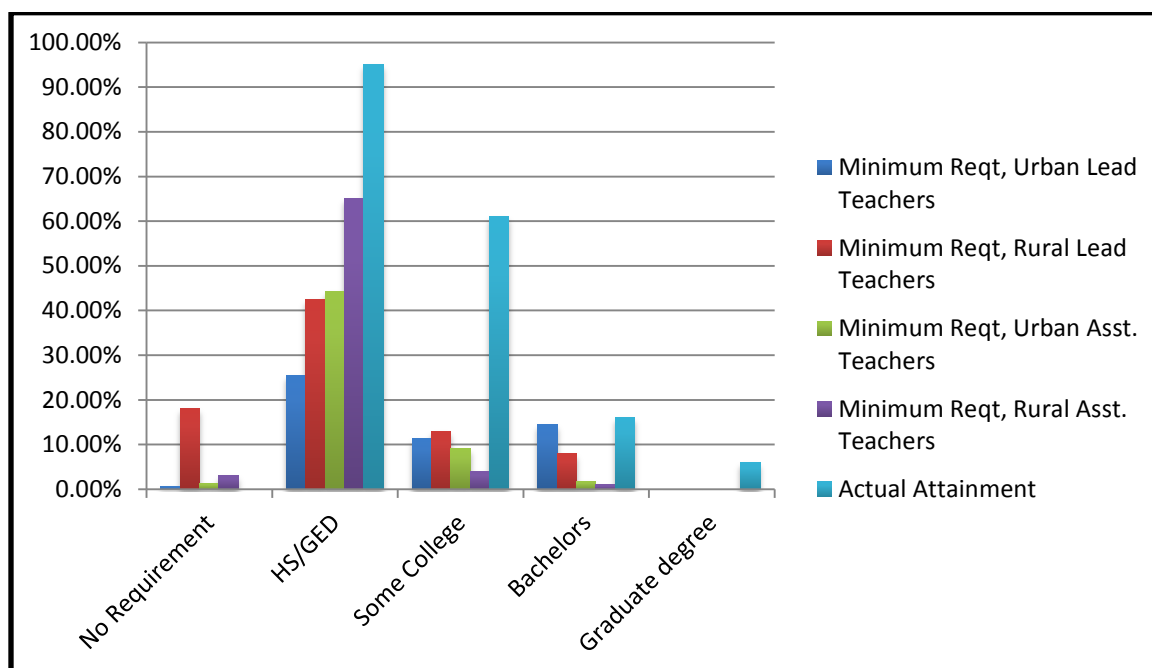
<sup>5</sup> For more information, see <http://www.earlychildhoodfinance.org/shared-services>.

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## APPENDIX

**Figure 1: Comparison of Employers' Minimum Teacher Requirements to Actual Educational Attainment**



## Figure 2: Median Annual Cost and Median Annual Revenue Compared<sup>6</sup>

These measures do not control for enrollment size or age distribution and so do not support any claims regarding relative cost of care per child. Overall, median revenue exceeded median costs, but profitability varied by type of provider. The median revenue minus median cost was highest among 5-Star providers, although median out-of-pocket costs for 5-Star providers understate true operation costs: More than half of the 5-Star providers in this sample did not report paying anything for facility rent or mortgage. Median measures for 2-Star providers and Santa Fe providers suggest that providers in those categories are more likely to experience costs in excess of revenues. This comparison is illustrated in the Figure above.

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<sup>6</sup> This is Figure 3-1 from the UNM 2010 Cost Report.

The following tables are from the UNM 2010 Cost Report

**Table 4-A: Median Annual Revenue by Source\***

	Star Level					Facility Type					
	1	2	3	4	5	Urban	Rural	Center	Family home	Group home	Santa Fe
<b>Tuition/fees paid by parents (n=107)</b>	7000	11,588	28,019	32,000	252,006	44,470	9,650	69,396	1230	85	69,000
<b>Tuition Paid by State or AIM High (n=98)</b>	2,000	27,867	63,599	42,134	131,564	27,866	16,545	80,628	0	2400	26,100
<b>Private Organizations including employers (n=81)</b>	0	0	0	0	0	0	0	0	0	0	0
<b>Child &amp; Adult Food Program (n=101)</b>	150	6,356	19,650	8,100	9,023	4,800	5,830	10,207	2,051	7,071	150
<b>Contributions &amp; donations (n=87)</b>	0	0	0	0	750	0	0	0	0	0	1,395
<b>Other (n=34)</b>	0	0	0	10	47,261	42	0	736	0	0	2,000

\*Two providers reported negative revenue, an indication that they did not understand that the question referred to gross revenue, not net profit. This is just one example of the difficulty with the data.

**Table 7-B: How was your program affected by the economic downturn? Responses given by 8 or more respondents**

	Star Level						Facility Type					
	Total	1	2	3	4	5	Urban	Rural	Center	Family home	Group home	Santa Fe
<b>Sample Size</b>	99	10	54	4	15	16	54	45	67	17	15	9
<b>Parents fell behind on pmts</b>	74%	60%	81%	50%	80%	56%	69%	80%	69%	82%	87%	22%
<b>Bought fewer supplies, materials</b>	69%	50%	76%	100 %	67%	50%	74%	62%	67%	82%	60%	44%
<b>Held back on raises, bonuses</b>	43%	40%	44%	50%	40%	44%	39%	49%	60%	0%	20%	44%
<b>Lay offs or reduced hours</b>	36%	40%	39%	25%	33%	31%	41%	31%	46%	0%	33%	67%
<b>Closed classroom(s)</b>	9%	10%	13%	25%	0%	0%	13%	4%	13%	0%	0%	22%
<b>Parents lost jobs so child withdrew</b>	8%	10%	9%	0%	0%	13%	7%	9%	1%	18%	27%	0%