The New Normal is Not Enough: Minnesota's Child Care Providers in Year 2 of the COVID-19 Crisis and Beyond

First Children's Finance

Contents

What We Heard About Family Child Care (FCC) & Access to Capital

Minnesota's child care providers have been through the wringer since 2020. Deemed "essential" by Governor Walz at the height of pandemic restrictions, child care providers stayed open to care for the children of essential workers. First Children's Finance, a Minnesota-based national nonprofit organization that provides loans, grants and business development assistance to child care businesses, partnered with the Federal Reserve Bank of Minneapolis to determine the effects of COVID-19 on the sector in 2021, and repeated the survey in 2022. This report analyzes 1,032 responses from the 2022 survey and performs some comparison with the previous year's study.

The survey indicated the following trends:

While the first year of the pandemic saw a dramatic drop in enrollment, the second year saw a rebound. This rebound, however, has only returned the sector close to pre-pandemic levels, which were already deemed "crisis" for the sector. Current remote working patterns have caused other unique challenges for enrollment.

Prior to the COVID-19 pandemic, Minnesota was short nearly 80,000 child care slots, with many facilities – especially in Greater Minnesota – maintaining months-long waiting lists. While demand has remained high, providers have struggled to meet it due to staffing challenges. While many have increased wages or offered bonuses, the historically low wages and challenging conditions of the sector have caused departure of longtime staff, as well as difficulty attracting new staff.

Increasing costs have been crushing to the industry and have caused providers to cut back in concerning areas. While nearly all respondents reported increasing costs across the board, 92% of respondents shared increasing costs related to food, and many indicated notable cutbacks in their ability to provide for children in their care. While some were able to sustain programs due to pandemic-related adjustments in food subsidy programs, many of those adjustments either have already ended, or are scheduled to end.

Nearly 86% of child care business respondents were recipients of state grant programs, most notably the Minnesota Child Care Stabilization Base Grants and Financial Hardship grants, funded by the American Rescue Plan Act. This funding allowed providers to maintain necessary staffing levels, keep tuition costs relatively affordable to parents and reduce reliance on high-cost financing options, which have been a challenge for providers in the past. However, many of these grants have ended, or are scheduled to end, and providers across the state indicated concerns about their ability to maintain services at current levels without increasing tuition costs, which they say are unsustainable to the families in their care.

Across Minnesota, the future is uncertain for child care providers. With rebounding demand, staffing challenges, increasing costs and state and federal funding scheduled to end, the sector is returning to its pre-pandemic crisis with new challenges. And the toll on providers themselves has been real: "I kept my doors open, however, I am now learning and feeling the personal toll [and] cost of this," reports a southeast Minnesota provider. "I do not know if I can restabilize financially by enrolling more children without support for the emotional and physical exhaustion of the past 2 years."

Introduction

> **Teaching children is hard and is the most important profession in building future generations.**

These words from a child care provider based in northwest Minnesota echo the sentiments of hundreds of child care entrepreneurs statewide. For years, access to quality and affordable early child care has been shown to provide not only positive outcomes for children, but also economic growth and stability in communities across the state[1] . While the importance and benefit of early child care is clear, the COVID-19 pandemic has continued to cause huge disruption for the already-uncertain industry of child care providers, business owners and the families they serve across the state.

Deemed "essential" by Governor Walz at the height of pandemic restrictions, child care businesses were asked to stay open to care for the children of fellow essential workers, even as most of their clients kept children at home amid lockdown regulations[2] . This caused unique economic challenges for providers – many of whom are small business owners running home-based businesses – that have rippled across a sector already navigating a challenging business model and unique supply and demand challenges pre-pandemic.

The sector was provided some assistance, primarily in the form of state grant opportunities, federal funding through the CARES Act, the more recent American Rescue Plan Act[3] and adjustments to food subsidy programs for meals. These programs have offered a cushion in a necessary and volatile industry, and helped many providers pay staff, keep their doors open and offer services to families in need. Yet these programs have end dates that are approaching or have passed. Many providers express concerns about their ability to maintain services at their current or previous levels, a level already considered inadequate to both the needs of their communities and the economic realities of being a small business owner catering to families with limited budgets.

As one of the nation's leaders in growing the supply and business sustainability of excellent child care, First Children's Finance sought to understand how the effects of the COVID-19 pandemic affected the sector in the State of Minnesota, as well as the business needs of providers in light of changing state funding opportunities. The organization, in conjunction with the Federal Reserve Bank of Minneapolis, conducted a survey of nearly 800 child care providers from all parts of the state in 2021. With results indicating worries as far-ranging as plunging enrollment, heavy use of high-interest financing, austerity measures and staffing concerns, the survey painted a concerning picture of a sector struggling to remain afloat despite some government and private sector interventions.

In 2022, First Children's Finance undertook another survey to help determine the current status of the industry and help paint a picture of what steps must be taken to help providers maintain and increase services as economic conditions begin to reveal a "new normal." This white paper provides an analysis of that survey, contextualizing hard data points amid comments from real providers and leaders within the industry, to give voice to the thousands of child care entrepreneurs who are keeping Minnesota families running.

Context/Organizations Involved

The two primary organizations involved in this study are detailed below:

First Children's Finance:

The mission of First Children's Finance (FCF) is to grow the supply and business sustainability of excellent child care. Founded in 1991, FCF is a national nonprofit organization based in Minneapolis, Minnesota, with regional offices in Iowa, Michigan, Minnesota and Vermont. FCF works to launch, stabilize, improve, and expand high-quality child care businesses, particularly those serving low- and moderate-income families. FCF provides financing, child care business training, consulting and coaching, and builds partnerships that connect child care businesses with the resources and expertise of the public and private sectors. FCF understands the issues and challenges child care businesses face in today's economy and in these wildly turbulent times. FCF has industry-specific expertise and a shared commitment to the success of high quality child care.

With a unique perspective, approach, and experience to providing business planning and financial assistance to child care entrepreneur clients, FCF approaches child care leaders as entrepreneurs, increasing their capacity to start and operate financially sustainable child care businesses.

The Federal Reserve Bank of Minneapolis

Established in 1941, The Federal Reserve Bank of Minneapolis is one of 12 Federal Reserve Banks across the United States. The Bank maintains a headquarters in Minneapolis, MN and a branch in Helena, MT. Responsible for the 9th District of the Federal Reserve, the Bank's area is composed of Montana, North Dakota, South Dakota, Minnesota, 26 counties in northwestern Wisconsin, and the Upper Peninsula of Michigan. The Bank conducts research and monitors regional economy to help determine the nation's monetary policy with an emphasis on 4 major areas: monetary policy, banking supervision, financial services and community development and engagement.

Definition of Terms

Many of these findings reference different types of child care businesses:

Family child care provider: Licensed family child care (FCC) providers care for infants, toddlers, preschoolers and school-age children, typically in their homes. In Minnesota, regulations limit the number of children in each family child care program to 10, 12 or 14 children, based on license type.

Child care center: Child care centers (CCC) provide care in groups based on age and are located in free-standing buildings, businesses, community centers or places of worship. In Minnesota, the number of children enrolled in a center varies and is regulated based on the number of staff, with different ratios of staff to children based on age.

For the purposes of this study, the State of Minnesota was divided into the following **sectors:**

7 County Metro Area:

Anoka, Carver, Hennepin, Scott, Ramsey, Dakota, Washington

Central:

Cass, Wadena, Crow Wing, Todd, Morrison, Mille Lac, Kanabec, Pine, Stearns, Benton, Sherburne, Isanti, Chisago, Wright

Northeast:

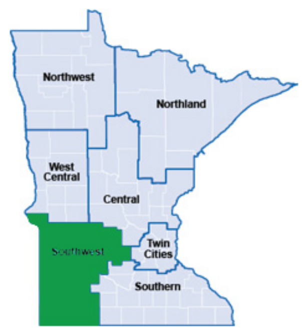
Koochiching, St. Louis, Itasca, Lake, Cook, Aitkin, Carlton

Northwest:

Kittson, Red Lake, Roseau, Norman, Lake of the Woods, Mahnomen, Marshall, Clearwater, Beltrami, Hubbard, Polk, Pennington

Southeast

Sibley, Waseca, Nicollet, Steele, Le Sueur, Dodge, Rice, Olmsted, Goodhue, Winona, Wabasha, Martin, Brown, Faribault, Watonwan, Freeborn, Blue Earth, Mower, Fillmore, Houston



Southwest:

Big Stone, Renville, Swift, McLeod, Kandiyohi, Lincoln, Meeker, Lyon, Lac Qui Parle, Redwood, Chippewa, Pipestone, Yellow Medicine, Murray, Cottonwood, Nobles, Rock, Jackson

West Central:

Clay, Grant, Becker, Douglas, Wilkin, Stevens, Otter Tail, Pope, Traverse

About the Data

The survey, titled Child Care Economic Recovery Survey, was conducted between April 11 – 24, 2022 and received a total of 1,032 responses. While the survey was not randomized and may not be a full representation of the child care industry, the number of respondents accounts for roughly 13% of licensed child care providers in the State of Minnesota.

The data skews heavily towards family child care providers, with 79% of respondents identifying as such. Nearly 17% of responses were from child care centers, and the remaining 4% are made up of programs like Head Start and preschools. The balance of family child care providers and child care centers in the survey closely aligns with the actual balance of programs in the state.

Geographically, sampling remains mostly consistent with distribution across the state, with some oversampling from central and southeast Minnesota. Just over 34% of responses came from the 7 County Metro Area, with the remaining coming from Greater Minnesota.

For providers who chose to report their racial/ethnic identity, 6% identified as racial and ethnic minorities, and 94% as non-Hispanic/white. While there is no publicly available data in Minnesota about the demographic diversity of child care business leadership, this breakdown aligns with past surveys. It is important to note, however, that this survey went to child care business leadership, which includes family child care businesses and center directors and owners. While this group tends to be primarily non-Hispanic/white, the broader child care workforce – including classroom teachers and aides - is a more diverse group.

Findings

Enrollment is stabilizing slightly but changing working habits are forcing other adjustments.

> **"..Families (are) starting to consider... less (child) care due to working at home.**

The COVID-19 pandemic, as might be expected, caused a significant decrease in enrollment in child care across the state. Virus concerns and changing work patterns caused families to pull their children from programs. While many providers kept their doors open through the height of the pandemic at the urging of the governor to care for the children of essential workers, survey results indicated that over 50% of all child care businesses reported a decrease in enrollment. It follows that the decrease in enrollment resulted in a significant decrease in revenue.

In the second year of the pandemic, providers began to see stabilization in their enrollment, with nearly 65% of respondents state-wide indicating either stability or a slight decrease in enrollment relative to the first 12 months of the pandemic shutdowns. This stabilization was most notable among family child care providers, where nearly 40% felt that their enrollment was beginning to stabilize. Yet the stabilization appeared to be at a lower level of enrollment than in pre-pandemic times. Concerned providers reported that changes in working habits – with more parents losing their jobs or working from home – have created what may be a lasting change, with some reporting more enrollment of "part time children" – children whose enrollment may match up with parental onsite work schedules and be a reduction of past hours – and an overall adjustment around the expectations for child care.

A central Minnesota provider was quite blunt: “My concerns are that families [are] starting to consider wanting less amount of care due to working at home. Families have left because of Covid closures.”

Where increases did occur, they were primarily in child care centers, with 36% noting more children attending their facilities. While this is a positive sign, the responses still indicate a return to pre-pandemic levels. These levels were already inadequate and deemed a “crisis” [4] due both to slots available to families and market pressures around tuition costs that providers can charge to parents, regardless of enrollment opportunities.

> “ ....We struggle to find qualified and experienced teachers which created [sic] a cycle of burnout and teacher turnover.

Demand remains high, in part due to lack of staff

Prior to the COVID-19 pandemic, Minnesota was short nearly 80,000 child care slots, with many facilities – especially in Greater Minnesota – maintaining months-long waiting lists, and many parents forced to drive hours to find a place for their children [5] . While enrollment stabilized or decreased, demand remained high; a lack of staff caused demand to outpace possible/potential enrollment.

Licensing requires that child care providers in Minnesota must maintain appropriate ratios between children and staff. In child care centers those ratios range as small as 1:4 for infants and 1:15 for school-aged children. Staffing remains the highest cost for most providers, which results in different expense for caring for different age groups of children. Infants remain the most costly to enroll and, from a business perspective, many providers view infants as a “loss leader:” families frequently enroll older siblings – who are less costly to care for - or build years-long relationships, where the initial costs are paid off in future tuition. This strategy was a reliable investment pre-pandemic, but the economics are decreasingly viable as the role of child care shifts to accommodate new parental needs and work.

Many family child care providers are sole proprietors and do not rely on additional staff to operate their facilities. However, child care centers, who typically hire outside staff to maintain operations, faced a tight labor market which constrains their capacity.

“We have always had a waiting list,” says a central Minnesota-based child care center leader with more than 20 years’ experience. “The problem is that I can’t get enough staff to take on more children than what we are already doing. I can’t pay staff enough to keep them here.”

Indeed, child care providers statewide indicated that staffing was a major barrier to increasing enrollment, and therefore business sustainability. Over 92% of respondents described finding and retaining qualified staff as either “difficult” or “very difficult.” This proved a significant increase from the previous year’s survey, and reflected broader national trends in the child care industry and beyond.

One Metro area provider summed it up clearly: “At the start of the pandemic I had 4 centers in operation, all at different stages of enrollment. We closed one center in November 2021 due to all the staff leaving.... Since our lease was due for renewal we opted not to renew. We struggle to find qualified and experienced teachers which created [sic] a cycle of burnout and teacher turnover.”

To recruit and retain staff, most centers surveyed indicated attempts at increasing wages or offering bonuses. Nearly 60% of child care centers report raising current staff’s salaries, and 28% indicate providing a bonus structure. Many centers have gone to other creative means, offering additional benefits that are not always found in this field, including paid time off, health insurance, retirement plans and even overstaffing classrooms to help avoid burnout. While these changes are beneficial to employees, they have come at a cost to providers; many of these businesses struggle to maintain stability and solvency. The director of a child care center in northwest Minnesota, who has seen a 15% increase in payroll costs in the last year, is concerned about the future: “We pay staff first, then our monthly payments after. There is nothing left over for the owner... We currently rely on the monthly grants to help fill the gaps. We can’t expect parents to pay 15% more to make up the difference, but when the grants run out we will have a problem.” These grants were commonly mentioned by providers as being a major factor in their ability to manage staffing levels.

Of all 1,023 survey respondents, only 4 described staffing as “easy” or “very easy.” For those who did indicate ease in staffing, most were located in the 7 County Metro and all cited grants, donors or loan resources as important to their continued success.

Costs are crushing, and in concerning areas

> **“Everything costs a lot more now**

While this sentiment was shared by a west central Minnesota family child care provider, it is indicative of responses from child care entrepreneurs across the state. Universally, the costs of running their businesses have increased significantly, and frequently in consequential and concerning areas.

Survey respondents were asked to identify cost changes in areas of their business including payroll, rent, utilities, maintenance and repair costs, transportation, supplies, learning materials, pandemic-related supplies, and food. Except for payroll and rent, where responses indicated stability or were inconclusive, all categories proved to experience modest or significant increases. While no category had less than 60% of providers indicating an increase, the most-selected category – with 92% of respondents indicating an increase, and 75% suggesting a significant one – was food costs for children.

“Grocery shopping is dreadful due to the prices, and they keep going up,” says a west central Minnesota family child care provider.

“The food program doesn’t come anywhere near covering food costs especially for fresh foods,” laments a northwest Minnesota provider.

“We stopped serving food when the pandemic began. Children bring their own lunches and snacks from home,” reports a Twin Cities-based child care center.

Child care entrepreneurs also expressed concern around increasing gasoline prices, which limits the number of trips they can take to the grocery store as well as the freshness of food. This led to additional food waste, which also increased due to absent or part-time attendees. These increases were especially notable for family child care providers, many of whom are not able to buy in bulk, and those in rural communities, who already face higher prices for food and fuel.

Many providers took advantage of food subsidy programs, such as the USDA’s Child and Adult Care Food Program. This program provides funding for food, reimbursing at a rate from a few cents to more than two dollars per student per snack or meal, and works on a tiered system based on income or geographic location. During the pandemic, providers were provided flexibility between tiers. Providers expressed concerns about planned reductions in flexibility and indicated that subsidies have not kept pace with inflation, causing significant hardships.

Beyond food, providers indicated pressing concerns around increases in pandemic-related supplies (83%), workplace supplies (83%), learning resources for children (79%) and maintenance (76%). Many of these are interconnected, with providers reporting needed repairs to play equipment, or replacement of toys and materials damaged by required cleaning protocols.

One unexpected finding, buried in many comments, is the recognition of the monetary costs of low staff morale, burnout, and the taxed mental health of workers. Dozens of providers note additional expenses around boosting staff morale and helping combat burnout, including breakfasts, coffees, gifts, and extra staffing. "Staff morale is not a financial expense but a *huge* factor in daily programming," cites a Metro-area Child Care Center director. "Having to move staff around to cover staff out, working longer hours to cover ratios [overtime] does not always compensate for being over worked."

Overall, the mounting costs have caused providers to make painful choices. "The cost to run my daycare keeps going up," indicates a family child care provider in southeast Minnesota, who has been in business for over a decade. "But I can't continue to put the extra cost on my daycare families [because] they can't afford child care the way it is. And the food program does not allow extra money either. And the cost of food keeps going up. I'm hardly breaking even. I love my job but I'm not sure how long I can afford to stay open."

"... I can't afford to raise my rates because most of my parents can't afford to pay for child care

Grants helped everywhere

Financing child care is a challenge, and providers have historically looked to tuition as their main source of revenue. The COVID-19 pandemic - and resulting disruptions - caused a precipitous drop in tuition across regions, which left providers struggling to meet business expenses, as well as their own personal finances. When asked whether their household income was impacted by financial losses in their child care businesses, most said yes. Over 70% of family child care providers answered affirmatively and nearly 40% of child care center owners did as well.

A Metro area provider, in business for over 30 years reported, "My rates are very low and affordable for parents because most are renters, and single parents. I can't afford to raise my rates because most of my parents can't afford to pay for child care."

Based on the 2021 survey, providers throughout the state were resorting to multiple means of financing, with many – notably family child care providers - opting for easy-access, higher-cost options like credit cards and pay-day loans. Cash flow options like these can pose a challenge, both from business and personal finance perspectives. A family child care provider in southwest Minnesota lamented in the 2021 study "Because we had to utilize credit cards during this time our credit has taken a hit. Now we can't even qualify for a 0% interest credit card ... If we were able to qualify for that it would be easier to get things paid back off." For her, having been in business for over 20 years, the solution seemed simple: "continued support from the State of Minnesota."

Thankfully, state support continued. While Minnesota utilized state funds to provide grants to child care providers during the pandemic, beginning in June of 2021, the Minnesota Department of Human Services provided a Child Care Stabilization Base Grant Program using federal funds from the American Rescue Plan Act to qualified providers that were licensed, open, operating and serving children during the funding period. The grants, calculated based on full-time equivalent (FTE) child care staff, included sole proprietors.

With monthly amounts up to $435 per FTE staff, the grants were available on a monthly basis, with a requirement that 70% be used to “increase compensation for staff regularly caring for children.” These grants were made widely accessible to providers who met eligibility requirements.

In addition to the Child Care Stabilization Base Grant Program, the state also designated a portion of American Rescue Plan Act funds to develop an additional grant opportunity to help providers experiencing extreme financial hardship. This program, called the Financial Hardship Grant Program, had different eligibility requirements and required a separate application and were not tied to continued employment of child care staff. Many respondents indicated receiving both types of grants.

These grants proved essential to providers remaining open, regardless of region or facility type. Over 86% of respondents reported receiving stabilization grants, which comments note were necessary for retaining staff and maintaining required ratios. It also helped keep doors open; of the 895 facilities surveyed that reported receiving grant money, only three reported closing permanently.

The continuation of these grants have led to a significant decrease in the use of high-cost financing options, notably among family child care business owners. Overall, there was a drop from 23% of respondents indicating use of these options in 2021 to 13% in 2022.

However, the emergency grant money comes with limitations. With primary restrictions on grants focused on employee payment, many providers did resort to increasing tuition to ensure solvency and absorb other expenses, which passed this burden along to parents and families. Due to more relationship-driven nature of their business models, far fewer family child care providers chose this route, with just under 20% reporting increased tuition. However, many providers were ambivalent about this, suggesting that currently-enrolled families may not be able to sustain further tuition raises in the future. That, coupled with the impending end of some grant programs in June 2023, has providers across the spectrum worried.

The director of a preschool in central Minnesota, noting the unknown future financial picture, finds herself in a quandary: “We don’t know if we can sustain increased wages once the grants end, so we’re going with bonuses. We also want to keep tuition affordable for parents.”

The future looks uncertain

> **“ I cannot afford to pay myself what I deserve after my time and effort**

The costs, cashflow challenges and funding streams have put child care providers across the state in a perilous circumstance. When asked about the future, providers express concern both for their businesses and for themselves.

“I cannot afford to pay myself what I deserve after my time and effort,” shares a family child care owner, working in southeast Minnesota. “I have a BA in early childhood [education] and cannot afford to pay myself $13 an hour.”

This concern was echoed across child care entrepreneurs, with 22% indicating that they were unable to pay themselves at times. When asked if their household income had been impacted, over 57% answered yes. The vast majority of providers who experienced a personal financial impact were family child care providers, who frequently rely on the direct income from tuition to maintain their own stability.

When asked how long providers believe they can stay in business, 18% indicated that their finances will allow for a year or less, while almost 60% suggested that they are unsure of their survival. That is a concerning level of insecurity across the sector, and consistent statewide, but most notable among family child care providers. The child care sector has been losing family child care providers for years, with too few new providers to fill the gaps that are created in communities. It seems unlikely that the sector will return to even the crisis conditions seen prior to the pandemic, and it must prepare for a "new normal."

Conclusion

With insufficient slots, changes in working habits from families, increasing costs and challenges finding staff, the current conditions of the child care sector remain bleak. While there has been stabilization in enrollment, the economic realities of the child care industry as it existed prior to the pandemic were already inadequate to meet the needs of Minnesota's families: not enough slots existed to meet needs, and providers are constrained in tuition costs due to the high expense of child care within family budgets. The rebound has returned the sector to what were already defined as "crisis" levels in a necessary industry.

Financial assistance from the state – notably Child Care Stabilization Base Grants, Financial Hardship Grants and flexibility in food reimbursement – proved a lifeline to most providers in 2022, allowing them to maintain baseline services, keep staff amid a challenging job market and handle rapidly-increasing prices caused by inflationary pressures. It also relieved pressure from use of high-cost financing options, which can have devastating long-term effects to providers personal circumstances. These circumstances combined allowed hundreds of child care businesses across the state of Minnesota to keep their doors open.

Yet, these programs have end dates. The Child Care Stabilization Base Grants are scheduled to end in June 2023, after which the financial realities of these primarily home-based and small businesses seem uncertain. With the majority of respondents indicating that they are unsure of their ability to maintain services into the future without continued assistance, the sector risks sinking deeper into the crisis-level conditions that have already caused inadequate availability for families and financial instability for providers.

The circumstances of the sector were summed up by a provider from southeast Minnesota:

"I think the trauma that has been experienced over the past 2 years by families, children and providers needs attention and concrete ongoing support. Ongoing Cohort based, facilitated, workshops to address the emotional labor and exhaustion of the past 2 years. I kept my doors open, however, I am now learning and feeling the personal toll [and] cost of this. I do not know if I can restabilize financially by enrolling more children without support for the emotional and physical exhaustion of the past 2 years. Thank you for this question. This is the first time I have been able to put that into words."

Endnotes

1 https://www.minneapolisfed.org/article/2003/early-childhood-development-economic-development-with-a-high-public-return

2 https://www.health.state.mn.us/docs/people/wic/localagency/wedupdate/moyr/2020/topic/0401covidcare.pdf

3 https://www.minnpost.com/state-government/2021/08/minnesota-is-getting-550-million-in-arp-money-to-help-its-child-care-industry-heres-how-the-state-is-spending-that-cash/

4 https://www.ruralmn.org/a-quiet-crisis-minnesotas-child-care-shortage/

5 https://mn.gov/deed/newscenter/publications/trends/september-2020/early-care-education.jsp