Higher education financial sustainability

An update

Reference OfS 2020.56

Publication date 11 December 2020

Contents

Summary

This report provides a summary of the Office for Students' (OfS's) analysis of financial data returned by registered higher education providers in England (excluding further education colleges) to the OfS at the end of October 2020 as part of an 'interim financial data return'.

This data return provided the first opportunity to analyse the impact of coronavirus (COVID-19) that providers expect to see on their financial performance and position in the financial years ended in 2020 (2019-20) and 2021 (2020-21), relative to the complete year prior to the coronavirus pandemic (2018-19).

Annex A contains charts which illustrate analysis of key financial performance and position data.

1. The aggregate financial position of OfS registered universities, colleges and other higher education providers is sound at the date publication of this report, with strong cash balances, despite the challenges faced as a result of the coronavirus pandemic.

2. The higher education sector in England has, in general, responded well to the pandemic with sensible financial management including good control of costs. In part, this reflects stronger overall student recruitment in 2020-21 than many were predicting. Although fee income from international students in 2020-21 is forecast to fall compared to 2019-20, it is still greater than in 2018-19.

3. To support financial resilience, borrowing has increased by around 5 per cent, including through some of the government-backed loan schemes. Further loan facilities have been agreed as contingency but have not yet been drawn down.

4. Although the aggregate financial position is sound, there is still very significant uncertainty as the pandemic continues, so the situation could change quickly. Issues that could impact on income include higher numbers of students dropping out, reduced income from accommodation and conference facilities or impact of COVID-19 restrictions.

5. As we have previously reported, there continues to be significant variability between the financial performance of individual providers. Despite this, the likelihood of multiple providers exiting the sector in a disorderly way due to financial failure is low at this time. We continue to monitor the financial position of individual registered providers and will continue to intervene if we consider that necessary to protect the interests of students.

Aggregate financial performance, income and expenditure trends

6. In aggregate, financial performance in 2019-20 is predicted to have been reasonable, particularly considering the significant disruption to operations during the year.

7. Total income is expected to have held up reasonably well, growing by 1 per cent in 2019-20 compared with the previous year. Prior to the national lockdown and suspension of some on-campus activities, total aggregate income had previously been forecast to grow by 3.6 per cent in 2019-20 compared to 2018-19. Whilst this forecast growth was not achieved, income was marginally higher than in the previous year and cash flow was broadly in line with 2019-20.

8. Aggregate income in 2020-21 is forecast to decline by approximately £700 million compared to 2019-20 and this is particularly applicable to overseas fee income (£626 million lower), donations and endowments (£219 million lower) and income from other income-generating activities, including catering and conferences, which is expected to be £228 million lower than in 2019-20.

9. Despite an overall more positive picture of student recruitment in the summer than might have been expected earlier in the pandemic, fee income forecasts are, in part, dependent on assumptions made by providers about in-year recruitment and retention of students through the year. Uncertainty about ongoing COVID-19 restrictions may affect these figures and change fee income expectations during the year. Income from course fees and educational contracts represents approximately 54 per cent of total aggregate income.

10. Tuition fee income from UK and other EU students is expected to increase overall year on year by a small amount in both 2019-20 and 2020-21 over previous years. While fee income from UK and EU students is increasing at a sector level, there is variability at individual provider level.

11. Overseas fee income is expected to have increased by 16.4 per cent in 2019-20, compared to 2018-19, reflecting the continued significant growth trend of recent years. However, at an aggregate level, providers anticipate this to decrease by 10.4 per cent in 2020-21 to £5.4 billion. Fee income from overseas students remains an important part of the financial model of the higher education sector in England.

Financial resilience, liquidity and borrowing

12. In general, providers have acted to find efficiencies and to reduce cash outflows, such as postponing capital expenditure, in response to financial risks during 2019-20 and in anticipation of continued financial risk in 2020-21. Reductions in cash outflows and increased focus on protecting future cashflows in the face of future financial challenges have, overall, strengthened aggregate liquidity at the end of 2019-20. This will improve the sector's resilience to financial risks in 2020-21. Liquidity is expected to decline by over 16 per cent in 2020-21, as a consequence of forecast decline in financial performance, but still remains strong at £10.3 billion.

13. Aggregate borrowing and other financial commitments are forecast to show a continued increase from £13.7 billion in 2019-20 to £14.2 billion in 2020-21.

14. Some providers have agreed short-term loan facilities with their bankers, such as overdrafts or revolving credit facilities, as contingent arrangements to support cashflow. Approximately £1.2 billion of these facilities remain undrawn at this time but are available, if needed, to support operations if significant risk scenarios materialise.

15. A small number of providers have utilised revolving credit facilities as part of their financial strategy, which is a matter of choice rather than necessity to sustain their operations.

Government backed coronavirus support schemes

16. During 2020, the government established various financial support mechanisms for businesses of different types and sizes to help mitigate the financial stress arising from coronavirus. A number of higher education providers have reported that they have entered into agreements to access financial support from government backed coronavirus loan schemes. These include the Coronavirus Corporate Finance Fund (CCFF), Coronavirus Business Interruption Loan Scheme (CBILS/CLBILS) and the Bounce Back loan scheme.

17. Approximately £1.24 billion of this support remains undrawn by providers and in place as contingency support in the event of significant financial risks in 2020-21.

18. Some providers may be eligible for additional financial support through the BEIS Sustaining University Research Excellent (SURE) scheme, which is calculated on forecast decline in overseas fee income.

Variation among providers

19. The sector's performance in aggregate does not, however, reflect the picture for individual providers. There continues to be a significant variation between providers and a widening spread of financial performance.

20. We are currently completing assessment of individual providers' data. Our work so far, and a review of the data submitted, indicates that overall – despite concerns early in the coronavirus pandemic about the income losses and financial risks – individual providers have been able to mitigate much of this through cost and cash management.

21. We are continuing to monitor the financial position of individual registered providers. For the vast majority of providers we are not currently concerned about short-term financial viability, although there is a small group of providers (a number in single figures) that we are monitoring more closely. Our judgement is that the likelihood of multiple providers exiting the sector in a disorderly way due to financial failure is low at this time.

Future risks and uncertainties

22. Financial forecasting is inherently more difficult in times of uncertainty and, despite positive news recently on vaccinations for coronavirus, there remains uncertainty about the operating environment for higher education providers in 2021.

23. Any further national or local measures that have a significant impact on providers' ability to deliver face to face learning are likely to affect income generated from on-campus activities, particularly from student accommodation, catering and conferencing. In pre-coronavirus times, this income was approximately 5 per cent of higher education provider income (£1.6 billion).

24. The impact of coronavirus on the longer term financial viability and sustainability of higher education providers is also uncertain. Many higher education courses are delivered over multiple years and the financial planning of providers is generally based on the cycle of students completing their courses over time. Any decline in student enrolments and fee income at individual providers, from one year to the next, is likely to mean that those providers will need to manage that income decline over the medium to longer term. The implications of coronavirus on fee income in 2020-21 on the financial management of providers will depend on the significance of the mitigating actions they have had to employ to protect their short-term viability.

25. There are a number of potentially significant events on the horizon, which will affect providers' financial viability and sustainability. For example:

- The 2020 Universities Superannuation Scheme pension revaluation exercise will re-open difficult debate about the financial sustainability of this and other pension schemes used by higher education providers and their staff. The affordability of increased employer pension contributions is uncertain and would increase financial pressure on providers in the future.

- 2020-21 is the final year that EU students can enter English higher education providers on the same fee and financial support terms as UK students. Aggregate EU tuition fee income has gradually declined since the 2016 referendum and in the run up to the UK's exit from the EU. The detail of the UK's future relationship with the EU will also have currently uncertain implications for other EU-related activities of the English higher education sector.

Annex A: Financial analysis charts – interim financial return

Notes on the data

1. **Years:** There are a variety of year end dates across providers, and so year data is sometimes referred to year 1, 2 and 3. For ease of reference, for the significant majority of providers this means 2018-19, 2019-20 and 2020-21 respectively. It should be noted that data submitted in the Interim financial data return for 2019-20 and 2020-21 is forecast and therefore unaudited.

2. **Tariff peer groups:** Three peer groups (non-specialist: high, medium and low tariff) are based on the tariff entry points of providers' undergraduate student population. The 'specialist: all' group includes providers offering specialist provision (a high proportion of students concentrated in a small number of subject areas) and regardless of tariff entry points. A fifth group (non-specialist: unclassified) consists of 23 providers with no tariff classification. This group includes a diverse range of providers with different financial structures and the aggregate data in this group can be skewed by data of a few individual providers.

Income

3. The aggregate data shows that the sector is expecting to report similar levels of income of £35 billion across all three years, albeit there is expected to be a decline in 2020-21. Table A1 shows the breakdown of income by source.

Table A1: Total income by source (£ million)

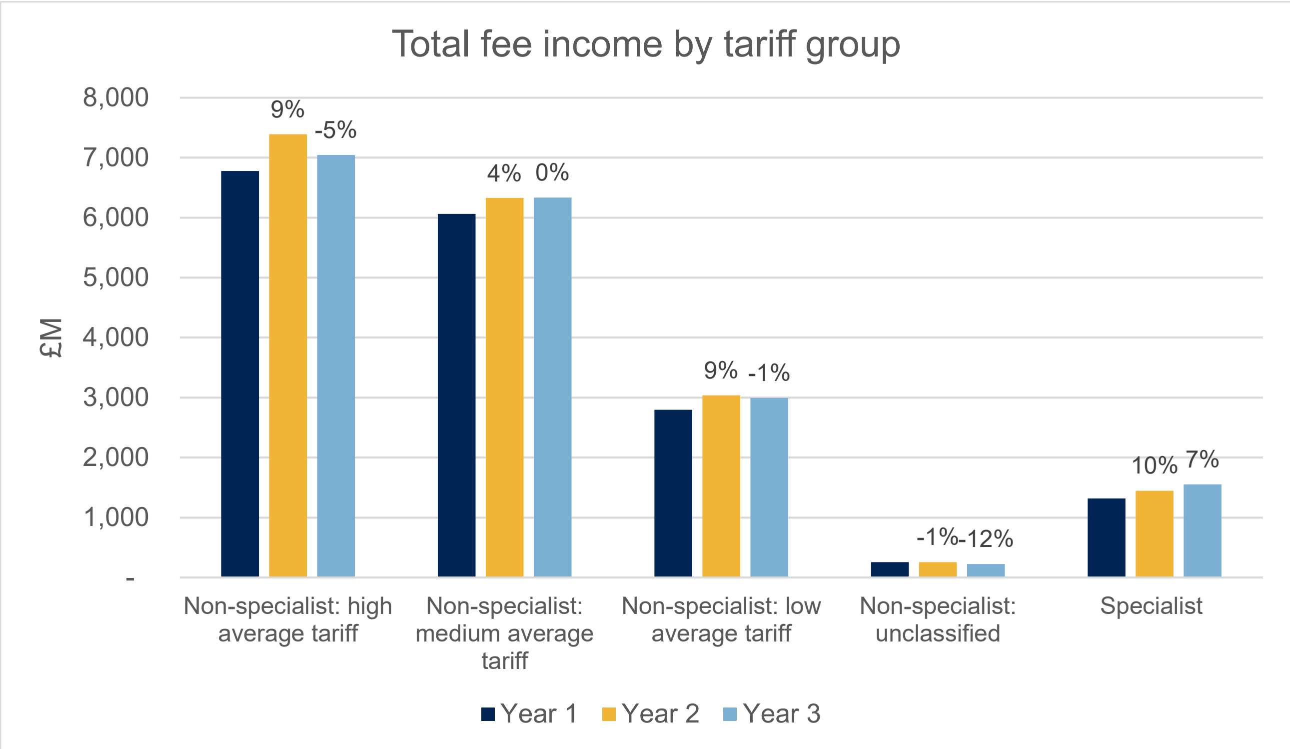
	2018-19 (Year 1)	2019-20 (Year 2)	2020-21 (Year 3)
Course fees and education contracts	18,236	19,334	19,087
Funding body grants	3,753	3,931	3,759
Research grants and contracts	5,386	5,197	5,411
Other income	6,940	6,289	6,061
Donations and endowments	715	690	470
Investment income	350	311	264
Total	**35,380**	**35,752**	**35,054**

Tuition fees

4. In 2019-20 total tuition fees were reported at £18.5 billion, an increase of 7.2 per cent compared with 2018-19 (£17.2 billion). Providers have forecast that this will fall by 1.7 per cent in 2020-21, although still remaining above 2018-19 levels. There is a trend of growth in the 18-year-old population in the near future which may provide opportunities for higher education providers to expand their student populations.

5. Figure A1 shows total fee income, split by provider tariff group. All tariff groups are reporting an increase between 2018-19 and 2019-20. Specialist providers forecast an increase between years 2019-20 and 2020-21, however all other tariff groups are anticipating a steady state or decline over the same period.

Figure A1: Total fee income by tariff group



Non-EU (overseas) fee income

6. Total non-EU (overseas) tuition fee income was reported at £6.0 billion in 2019-20, an increase of 16.4 per cent compared with 2018-19 (£5.2 billion). At an aggregate level, providers anticipate this to decrease by 10.4 per cent in 2020-21 to £5.4 billion. All tariff groups are forecasting an increase between 2018-19 and 2019-20.

7. Between years 2019-20 and 2020-21, all tariff groups forecast declines:

- non-specialist: high -12.6 per cent (-£457.8 million)
- non-specialist: medium -9.9 per cent (-£129.4 million)
- non-specialist: low -2.3 per cent (-£11.0 million)
- non-specialist: unclassified -14.9 per cent (-£33.1 million).

8. The specialist group of providers anticipates a small increase of 1.3 per cent (£5.0 million).

9. Fee income for different tariff groups is shown in Table A2.

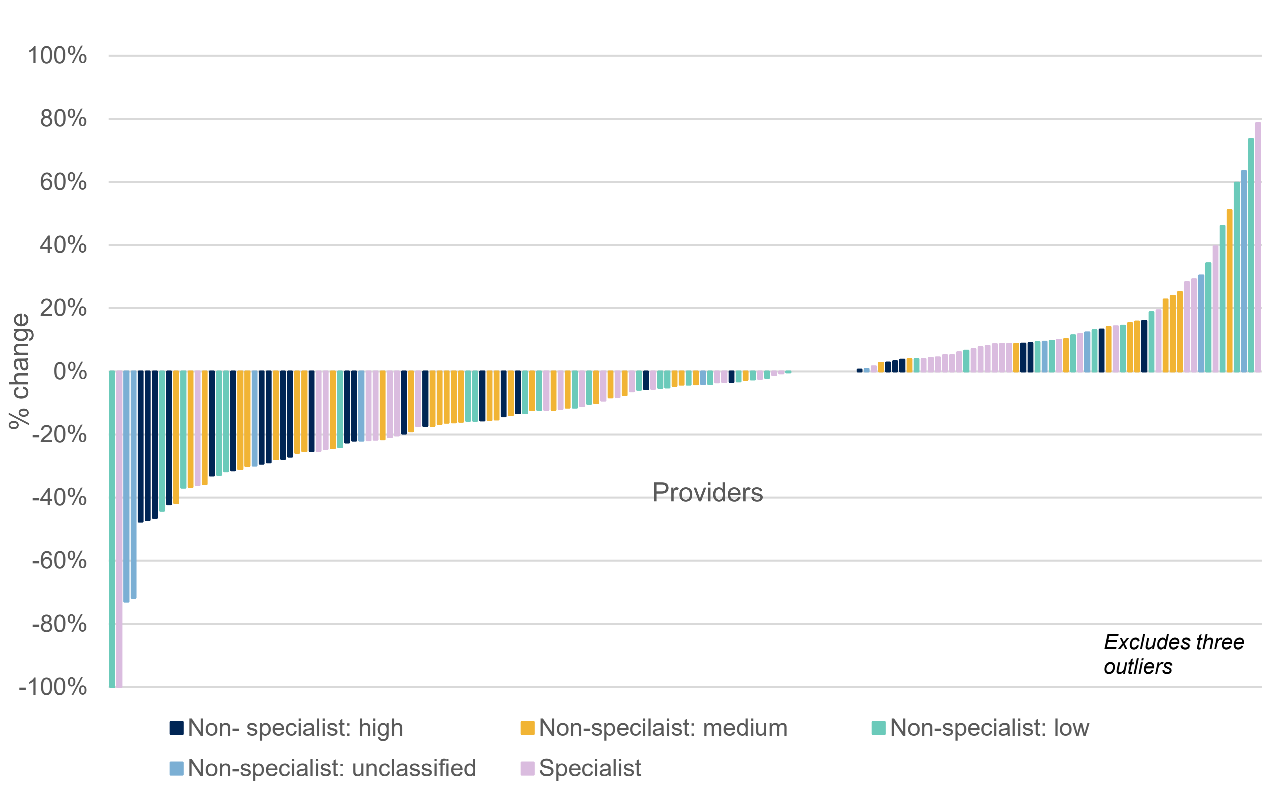
Table A2: Non-EU (overseas) fee income (£ million)

	2018-19	2019-20	2020-21	Change 2018-19 to 2020-21	% change
Sector (£ million)	5,163	6,010	5,384	221	4.3%
Non-specialist: high average tariff	3,107	3,628	3,170	62	2.0%
Non-specialist: medium average tariff	1,148	1,303	1,174	26	2.2%
Non-specialist: low average tariff	366	469	458	91	24.9%
Non-specialist: unclassified	206	222	189	-17	-8.4%
Specialist	335	389	394	59	17.6%

10. The aggregate trends on income from overseas fees does not apply to all providers and there is a wide range of expectations.

11. Figure A2 shows the variation in expected overseas fee income at each provider between 2019-20 and 2020-21, highlighted by tariff group. This ranges from a decline of 100 per cent to an increase of 79 per cent. 48 providers are reporting an increase in overseas fee income over the period, 3 providers anticipate no change and 79 a decline. There is a variable pattern of change across each tariff group.

Figure A2: Overseas fee income change between 2019-20 and 2020-21 (where non-EU fee income is over 5% of total fee income)



Total expenditure

12. The aggregate data on expenditure is distorted in 2018-19 and 2019-20 by a significant pension cost adjustment. This is an accounting entry and inflates total expenditure by £4.1 billion in 2018-19 and deflates expenditure by £2.2 billion in 2019-20 – a swing of 6.3 billion between the two years.

13. Removing these adjustments to aid comparability between years, total expenditure is expected to have increased by 2.9 per cent in 2019-20, predominantly in staff costs which represents approximately 55 per cent of total expenditure (adjusted for the pension adjustment). Total expenditure is forecast to increase by 1.7 per cent in 2020-21. Expenditure for the three years, both with and without pensions adjustment, is shown in Table A3.

Table A3: Expenditure

Total expenditure (£ million)			
	2018-19	**2019-20**	**2020-21**
Staff costs (excluding pension adjustments)	17,976	19,008	19,239
Other operating expenses	12,799	12,505	12,976
Depreciation and amortisation	2,292	2,380	2,451
Interest and other finance costs	730	838	652
Restructuring costs	111	140	151
Total expenditure (excluding pensions adjustment)	**33,900**	**34,872**	**35,467**
Pension adjustments	4,119	-2,158	558
Total expenditure	**38,019**	**32,714**	**36,025**

Cashflow from operating activities

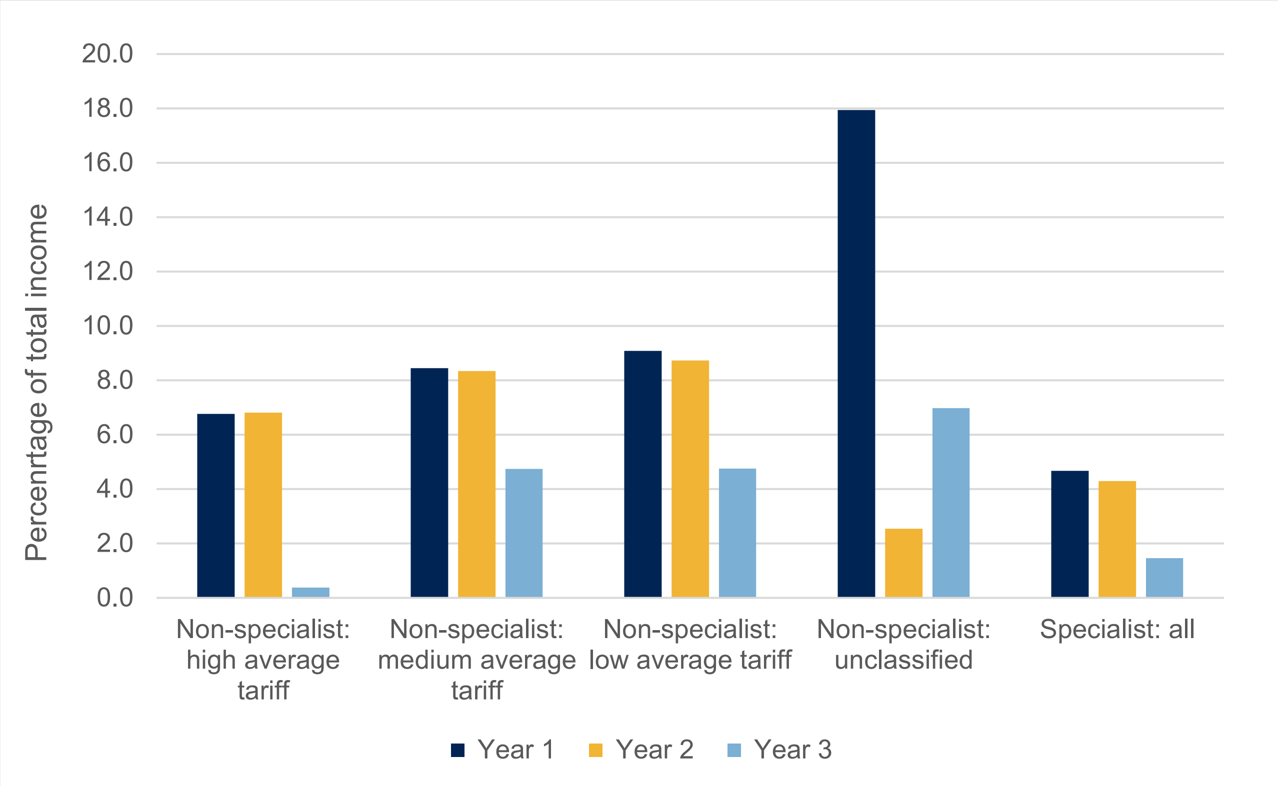
14. Operating cashflow measures a provider's net cash generated from its operations to meet day-to-day obligations – this is the cash that a provider generates from its core business activities, such as teaching and research, after paying its usual costs, such as salaries and other operational expenses.

15. At an aggregate level, operating cashflow is expected to decline from £3.1 billion in 2018-19 (7.4 per cent of total income) to £3.0 billion in 2019-20 (7.2 per cent of income). A further, more significant, decline is expected in 2020-21, where the sector is projecting operating cashflow to fall by 59.2 per cent to £1.2 billion, equivalent to 2.2 per cent of income.

16. Figure A3 shows the level of operating cashflow (after debt servicing costs) as a percentage of total income by peer group in 2018-19 to 2020-21. Cashflow from operating activities varies considerably between providers and tariff groups.

17. Figure A3 shows that most tariff groups reported a steady state or marginal decline in levels of operating cash flow in 2019-20 compared with 2018-19 with more substantial declines expected in 2020-21. The steepest declines are expected in the Non-specialist high tariff group (reducing from 6.8 per cent in 2019-20 to 0.4 per cent of income in 2020-21) and the specialist tariff group (reducing from 4.3 per cent in 19-20 to 1.5 per cent of income in 2020-21). The non-specialist unclassified tariff group is an exception to this trend, showing a steep decline in 2019-20 followed by an increase in operating cash flow in 2020-21.

Figure A3: Cashflow from operating activities as a percentage of total income



Surplus (adjusted)

18. Surplus levels show a provider's ability to generate income above its accounting costs. Generating surpluses over time is important to enable a provider to invest in future sustainability (e.g. infrastructure and academic quality) and protect against financial risk.

19. Accounting treatments can sometimes distort movements in surplus levels between years, making it difficult to use overall surplus as an indicator to assess underlying financial performance.

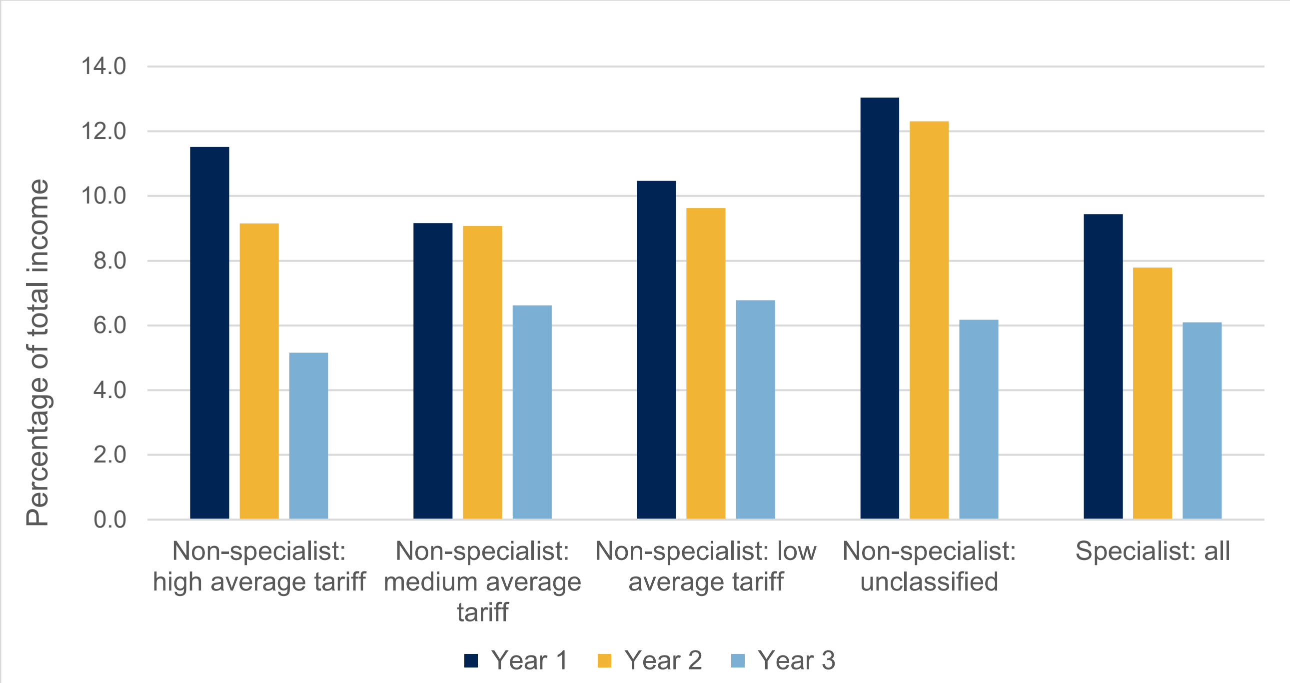
20. In 2018-19 and 2019-20, the sector reported significant non-cash pension adjustments following the 2017 and 2018 Universities Superannuation Scheme (USS) valuations, as well as accounting adjustments relating to other defined benefit pension schemes. Whilst the financial sustainability of pension schemes is an important concern for the sector, the resulting impact of these particular accounting entries on surplus levels is not reflective of the underlying financial performance of the sector in those particular years.

21. To aid comparability, excluding these pension scheme accounting adjustments from total expenditure, the sector's surplus levels are expected to fall from £3.8 billion in 2018-19 (10.7 per cent of income) to £3.3 billion (9.1 per cent of income) in 2019-20, and to £2.0 billion (5.8 per cent of income) in 2020-21.

22. Figure A4 shows the level of surpluses (excluding pension scheme impacts) as a percentage of total income by peer group for 2018-19 to 2020-21. This chart shows surplus levels declining in both 2019-20 and 2020-21 across all tariff groups, with the greatest declines expected in the Non-specialist high average tariff group, where surpluses are forecast to fall from 11.5 per cent

in 2018-19 to 5.2 percent of income in 2020-21 and the Non-specialist unclassified tariff group, where surpluses are forecast to fall from 13.0 percent in 2018-19 to 6.2 per cent of income in 2020-21.

Figure A4: Surplus (excluding pension scheme adjustments) as a percentage of total income by tariff group



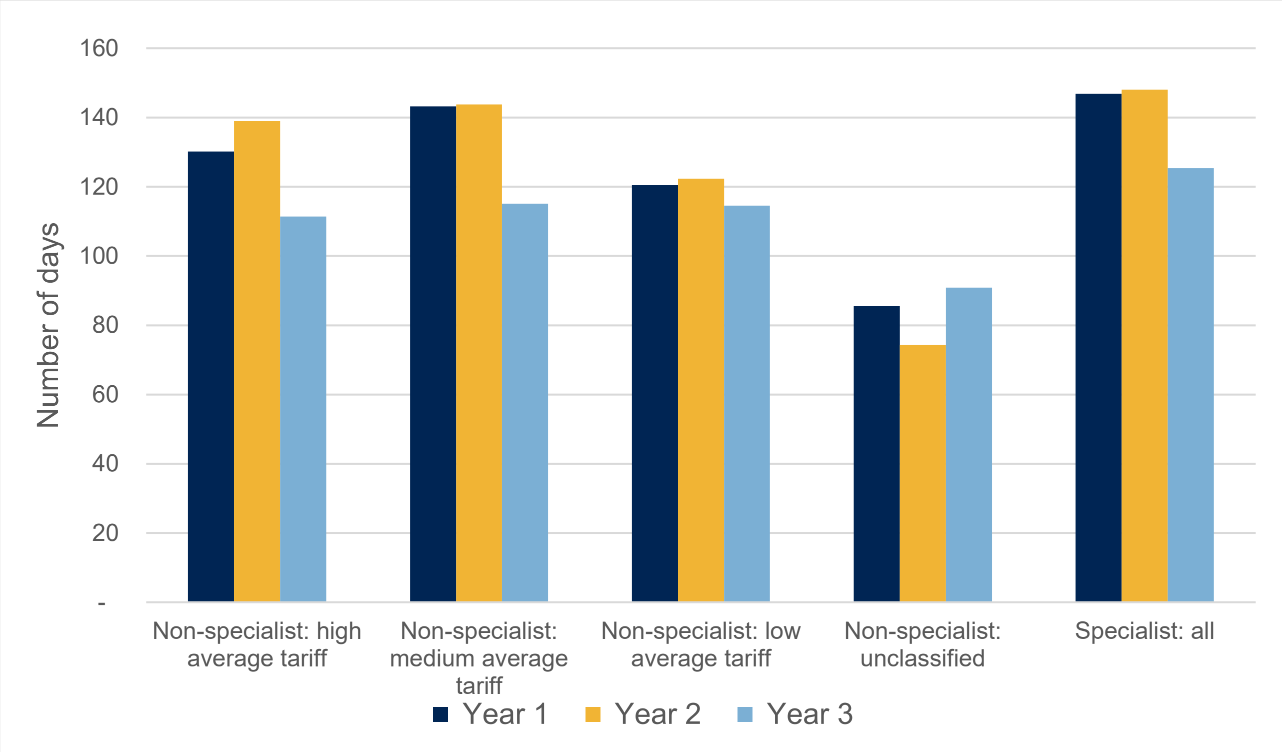
Liquidity

23. 'Net liquidity' is cash and liquid investments, and 'net liquidity days' shows the number of days from the financial year end for which a provider is able to pay its day-to-day expenses from the cash that it holds in its bank account and any short-term investments (such as an investment savings account or short-term bond).

24. Reductions in cash outflows in 2019-20, such as spending on capital projects, and an increased focus on protecting future cashflows to manage future financial risk and uncertainty, has resulted in stronger cash holdings and a rise in net liquidity: from £11.5 billion at the end of 2018-19 (133 days' expenditure) to an expected £12.3 billion (138 days) at the end of 2019-20. However, net liquidity is expected to decline to £10.3 billion by the end of 2020-21, equivalent to 114 days of expenditure.

25. Figure A5 shows the level of liquidity as a percentage of total income across tariff groups for 2018-19 to 2020-21. This chart shows that most tariff groups reported increases in liquidity days in 2019-20 compared with 2018-19 (increases ranging from 1 to 9 days), with declines of expected across these groups in 2020-21 (between 7 and 29 days). The non-specialist unclassified tariff group is an exception to this trend, showing a decline in 2019-20 and an increase in 2020-21.

Figure A5: Liquidity days by tariff group



Borrowing and other financial commitments

26. Aggregate sector borrowing includes both short- and long-term financial commitments, including loans from directors and shareholders, as well as from other sources such as banks and bonds.

27. At the end of 2019-20, sector borrowing was £13.7 billion (equivalent to 38.4 per cent of income), a rise of £0.7 billion compared to 2018-19. Forecasts show that the sector is projecting borrowing to continue to rise to £14.2 billion by the end of 2020-21 (40.6 per cent of income). This is a slower increase in borrowing than in previous years.

28. Table A4 shows the forecast results borrowing at the end of 2020-21 broken down by quartile, average and median value.

Table A4: Borrowing as a percentage of total income – forecast at year-end 2020-21

	Sector	Non-specialist: high average tariff	Non-specialist: medium average tariff	Non-specialist: low average tariff	Non-specialist: unclassified	Specialist
Total (£ million)	14,241	8,715	3,161	1,522	142	702
Average (%)	40.6	46.9	34.9	38.0	31.7	23.5
Lower quartile (%)	0.2	29.6	18.2	0.0	0.0	0.0
Median (%)	22.6	48.7	28.3	15.7	0.7	7.4
Upper quartile (%)	44.1	60.5	44.1	36.1	41.4	35.5