

THE CONVERSATION

Hard Evidence: are universities strapped for cash?

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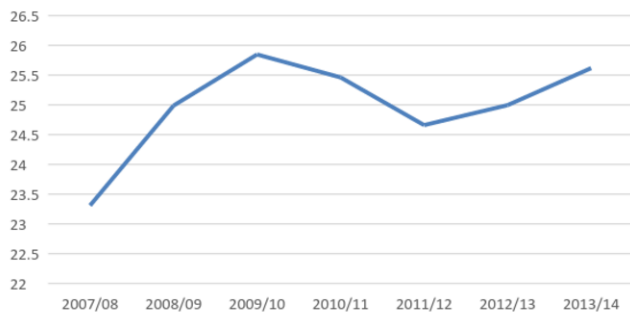
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Are universities counting their pennies? Education fund via Lucian Milasan/www.shutterstock.com

English universities have known since June that there would be cuts to higher education funding. Now the amount and detail of the savings have been disseminated to universities: the sector must make a total saving of £150m. Some have argued this is evidence that the sector is in “perpetual financial crisis”. So what are the likely impacts of the latest round of cuts on universities and how will they manage their finances?

At first sight, the English higher education sector seems to have had reasonably steady income over the last few years. As the first graph below shows, in the period after the financial crisis, universities' real income initially rose. Despite a dip between 2009-10 and 2011-12, it has been slowly rising since but has yet to recover to pre-2010 levels.

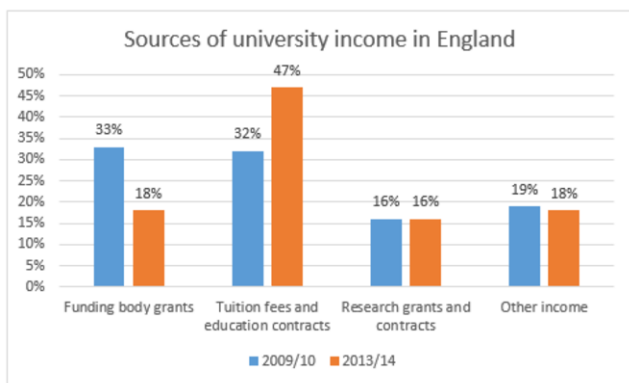


Income of English universities, £ billions. HESA, Finances of Higher Education Providers, Author provided

Prepare for volatility

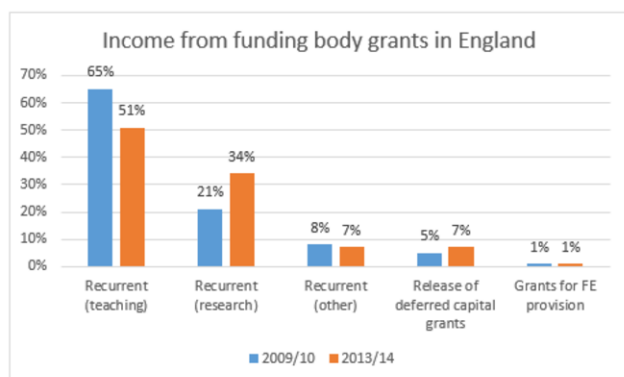
It is important to look at the detail of where the £150m of cuts will now fall. The savings are to be made in the 2015-16 financial year (April to March), which overlaps two academic years 2014-15 and 2015-16. This means that universities are suddenly having to deal with a loss of income which they had expected to receive for both for the current academic year and the next. Government funding, which has historically provided universities with financial certainty and stability, is no longer a reliable source.

All cuts will come from the recurrent teaching grant, while universities' grant for research will remain ring-fenced. Let's take a step back and see how the importance of the recurrent teaching grant has changed in the composition of universities' income over the past few years. From the second graph below we can see that in 2008-9, grants from funding bodies, which for English universities comes largely from the Higher Education Funding Council for England (HEFCE), were 33% of the sector's total income. By 2013-14, following the introduction of undergraduate tuition fees of up to £9,000 a year in 2012-13, this percentage had dropped to only 18%.



HESA, Finances of Higher Education Providers, Author provided

At the same time, the money set aside for teaching within grants from the funding body has fallen from 65% of the total in 2008-9, to 51% in 2013-14, as the third graph below shows.



HESA, Finances of Higher Education Providers, Author provided

Gauging student demand

The flip-side of this is that tuition fees have become more important – rising from 32% of English universities' income in 2008-9 to 47% in 2013-14. This move means universities are ever more open to the vagaries of market demand. Tuition fees come from undergraduate and postgraduate courses, both from home and EU students and those from overseas.

These overseas students have been a particularly lucrative source of income for universities as there is no cap on their numbers or the fees that they can be charged. But the overseas market is becoming increasingly competitive (for example, there was a 2% drop in international students in the UK between 2011-12 and 2012-13) and this source of funding is becoming less predictable.

Because of this, the domestic student market is becoming more and more important to universities. But population changes in the UK mean that there will be fewer 18-20 year olds to take up places at university – a fall of more than 12% in 18-24 year olds is forecast between 2012 and 2021. So the tuition fee income on which universities have become much more reliant is, like government funding, likely to be volatile.

The chancellor George Osborne's decision to lift the cap on the number of students each university can admit, which comes into effect from September, could offer a glimmer of hope for universities. Universities can now recruit as many extra students as they want with the appropriate qualifications. When the plans were announced, it was originally intended that any extra student recruited would mean that the university would receive both the tuition fee and the usual associated HEFCE funding allocated to each student.

However, if we look at the detail of the £150m cuts, as set out in the table below, we can see that the money set aside by HEFCE for the increase in student numbers has been cut to achieve the overall saving.

Source of saving	£ millions
Previously set aside for student numbers increase	37
Penalty for over-recruitment	10
Catalyst fund	13
Transitional research funding from teaching sources	52
2.4% decrease in teaching recurrent grant for 2014-15	38
Total	150

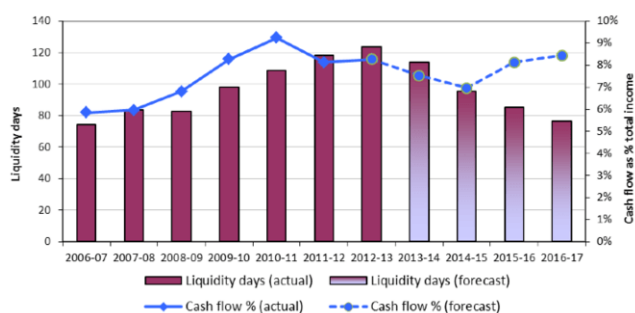
Sources of HEFCE's savings HEFCE, Author provided

So universities can indeed increase the numbers of students they enrol (for example,

through the clearing process after A-Level results are announced in mid August) – but institutions will only receive the tuition fee for these extra students, rather than any government funding. In the short term, at least, the temptation for universities will be to recruit extra students only from low-cost subjects, such as the humanities, to cross-subsidise students in the high-cost subjects, such as science.

Test of resilience

The higher education sector is in a potentially precarious situation with possibly large fluctuations in demand (and hence funding) from one year to the next. Are universities resilient enough to withstand these fluctuations? HEFCE's own forecasts of the financial health of the sector between 2013-14 and 2016-17 emphasises the need for strong liquidity – the number of days for which a university's cash reserves would cover their expenditure. As a sector, liquidity has strengthened over the recent years of uncertainty, as the graph below shows, but the forecast is for this to fall and for borrowing to increase. As HEFCE points out, this is “an unsustainable trajectory”.



Net liquidity and cash flow 2006-7 to 2016-17 HEFCE's
Financial Health of the Higher Education Sector: 2013-14 to
2016-17 Forecasts

Perhaps more worrying, is that the picture for the overall sector conceals vastly different effects for different universities when it comes to student demand. Although the average increase for the sector in both domestic and EU students between 2012-13 and 2016-17 is predicted to be 5.5%, some universities could see numbers decline by more than 20%, while at others they could increase by more than 40%.

The irony of these cuts, however, is that they fly in the face of the laudable proposals made in June by the universities minister, Jo Johnson, for universities to be ranked and rewarded for their teaching excellence. Paradoxically entitled: “Teaching at the heart of the system”, Johnson’s speech announced the development of a new Teaching Excellence Framework to shore up the quality of university teaching.

Yet teaching quality will be the first casualty of the changing funding regime as the lack of certainly in long-term planning will lead universities, in pursuit of flexibility, to employ more staff on short-term contracts. Some may even consider closing departments which experience dips in student demand and cannot be sustained.



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