



Scottish Funding Council
Comhairle Maoinachaidh na h-Alba

The Financial Sustainability of Colleges and Universities in Scotland – Review Report

SFC Publication

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LEADING, INSPIRING, INVESTING

We are the national, strategic body that funds further and higher education and research in Scotland.

About us

We invest in education that is accessible to learners from all backgrounds, gives them a high-quality learning experience, supports them to succeed in their studies, and equips them to flourish in employment, further study and fulfilling lives.

We invest in excellent research and innovation that adds to current knowledge, delivers economic and societal value, enhances Scotland's international reputation and attractiveness, and makes the world around us prosperous, healthier and more sustainable.

We ensure our autonomous colleges, universities and specialist institutions form part of a successful, world-leading, coherent and sustainable system of education that responds effectively to the future needs of learners and the skills needs of the economy and society, enhances our rich cultural life, and strengthens Scotland's international connections.

We will be an excellent, outcome-focused public body that provides leadership, inspires confidence, models collaborative working, is committed to continuous improvement, and stewards public resources well.



WE INVEST

£1.9BN

IN SCOTLAND'S 26 COLLEGES, 16 UNIVERSITIES AND 3 SMALL, SPECIALIST INSTITUTIONS



WE SUPPORT ALMOST
500,000
STUDENTS EACH YEAR

OUR RESEARCH EXCELLENCE GRANT HELPS TO GENERATE ALMOST

£800M

OF ADDITIONAL RESEARCH INCOME



OVER THE PAST 10 YEARS WE HAVE INVESTED **£1.8BN** IN COLLEGE AND UNIVERSITY ESTATES



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The Financial Sustainability of Colleges and Universities in Scotland

Introduction

1. The financial sustainability and viability of Scotland's colleges and universities is vital for our pipeline of talent for the economy, to protect and enhance our research and science base, to safeguard jobs within the sector, and to respond effectively to the national mission on social and economic recovery. We last reported on the overall financial sustainability of Scotland's colleges and universities in February of this year¹, before COVID-19 had impacted on their operations. At that point, we highlighted the challenges facing Scotland's colleges and universities and the risks they faced, and we emphasised the importance of institutions adapting to future changes in the environment.
2. The COVID-19 pandemic has impacted profoundly on the environment in which Scotland's institutions operate, the teaching methods employed, and the whole student and researcher experience. Maintaining short-term liquidity remains a significant challenge, alongside navigating this period of great uncertainty. We have worked closely with the Scottish and UK Governments on urgent actions to support institutions through their financial sustainability and liquidity challenges in the short-term, all of which are set out below.
3. This report presents an aggregate picture of the financial health of Scottish institutions, mainly based on an analysis of the most recent financial forecast information reported to us by each institution. It also refers to the baseline position of the institutions pre-COVID, which was set out in the report on the [2018-19 annual accounts](#), and the forecast position of both sectors at an earlier stage of the pandemic.
4. The figures presented in this report are subject to ongoing change as the environment changes and as governing bodies plan and make choices and decisions about the future accordingly. It is important to note that, while this report presents an aggregate picture, there is significant variation in the financial position of individual institutions. We will continue to engage with institutions about the robustness of their projections and future plans in this new world and provide regular updates.

1

http://www.sfc.ac.uk/web/FILES/corporatepublications_sfccp022020/SFCCP022020_The_Financial_Sustainability_of_Colleges_and_Universities_in_Scotland.pdf



Financial sustainability of colleges

5. The financial sustainability of the college sector is very fluid, with assumptions being updated as circumstances change. All of the figures in this section capture incorporated and non-incorporated colleges.

Key messages

- Colleges were facing specific financial challenges prior to the impact of COVID-19, for example increasing cost pressures from cost of living pay awards, employers' pension contributions, maintaining the college estate and the UK's exit from the European Union, and were already implementing transformation plans to address those challenges. While colleges are undertaking detailed scenario planning work and the position on the longer-term impact continues to develop, the COVID-19 crisis has heightened those challenges, particularly for colleges with high levels of commercial income.
- Maintaining short-term liquidity remains colleges' main challenge, with three colleges forecasting negative cash balances by the end of July 2023.
- The sector is forecasting an adjusted operating deficit up to 2020-21. While there could be a return to marginal surpluses in later years, this is dependent on SFC funding for staff restructuring costs, without which operational shortfalls would be reported in all years. The sector-wide position masks particular financial challenges for some individual colleges.
- Several colleges have delayed the implementation of voluntary severance programmes as a result of COVID-19. These programmes were being taken forward by colleges in order to secure their financial sustainability prior to the outbreak of COVID-19.
- Coronavirus Job Retention Scheme (CJRS) income arising from furloughing of staff has been insufficient to offset the projected loss of income.
- It is anticipated that the impact of COVID-19 will be felt most severely in 2020-21.

Actions to date

Emergency response for 2019-20 & 2020-21

- **Targets:** We confirmed that we would not recover funds for shortfalls against outcome agreement targets (including core student number credit targets) where these are related to COVID-19 for AY 2019-20. We subsequently confirmed the same position for AY 2020-21.
- **Reporting requirements:** We are keeping returns and reporting requirements to a minimum, focusing on absolute priorities to ensure continued compliance with legislative requirements.
- **Student Support:** At the beginning of lockdown, SFC arranged for some of the AY 2019-20 (April-July 2020) college student support allocations to be brought forward and paid out in Financial Year (FY) 2019-20 (March 2020), where requested, so that colleges had access to funds required to be able to make awards immediately to students facing increased financial hardship. For AY 2019-20 we also:
 - Provided flexibility to colleges to redirect travel and childcare funds to discretionary funds.
 - Removed the individual student £4,000 cap on discretionary funds.
 - Provided flexibility to allow colleges to bridge the gap between the end of student support funding when a student's course finished (at the end of the AY) and the availability of benefits where students were unable to secure employment.
- **One-plus activity:** For 2019-20 SFC removed the 2.5% limit for 'one-plus' activity (where students undertake more than one full-time course/ programme over the AY) to enable students to benefit from additional learning during the lockdown period. We also confirmed that credits were claimable for timetabled guidance on college sector higher education (HE) programmes and we updated our credit guidance to reflect this position.
- **College Credit Guidance:** For 2020-21 our published Credit Guidance enables colleges to claim credits for students who need to repeat units as a result of COVID-19 (deferred students). As a consequence, we removed references to 'one-plus' activity. In order to help colleges shift their provision to allow for additional demand for mainstream provision aimed at future skills areas and providing shorter retraining, reskilling and upskilling courses, we have required colleges to deprioritise:
 - School/college activity outwith senior phase.

- Additional units to full-time FE students, unless they are in response to COVID-19 (i.e. deferred units or deemed essential in terms of future employability or progress to HE).
- **Capital funding:** In August, SFC announced £2.3 million of additional capital funding for colleges in FY 2020-21 to support the provision of ICT equipment for learners to help tackle digital poverty. In addition, SFC announced £6.5 million of additional capital funding to support the economic recovery in FY 2020-21.
- **Flexible Workforce Development Fund (FWDF):** SFC has extended the timescales for the expenditure of AY 2019-20 FWDF by 12 months. The AY 2020-21 FWDF programme budget has been increased by £3 million to £13 million.
- **Youth Guarantee Programme (YGP):** Designed to give all young people access to work, training, education or formal volunteering. Of the £60 million total for YGP, colleges have been directly allocated £10 million and may also benefit from indirect funding.
- **Transitional Training Fund:** A £25 million fund that has been developed to support those facing redundancy. It is anticipated that colleges will play a key role in the operation of this fund.
- **Coronavirus Job Retention Scheme (CJRS):** Colleges were eligible to apply to the UK Government scheme. CJRS funding is included in the forecasts captured in this report.
- **Cash advances:** SFC has provided flexibility in grant drawdowns to several colleges encountering liquidity challenges.

Additional responses

- We are working with the Scottish Government and stakeholders on a possible Transformation Investment Fund to support colleges to make specific one-off investments to achieve lasting improvement in their financial health.
- We are undertaking a review of coherent provision and [sustainability](#).
- We are reassessing our regulatory, data and reporting requirements.

Annual Accounts 2018-19 (baseline year)

Colleges were facing specific financial challenges prior to the impact of COVID-19.

6. A full analysis of the 2018-19 financial position of the college and university sectors, as shown in the financial statements, can be found on [SFC's website](#). This analysis presents an aggregate picture of the financial health of Scottish colleges based on a review of the 2018-19 annual accounts of the twenty incorporated and six non-incorporated colleges. While the analysis presents an aggregate position, there is significant variation in the financial position of individual colleges.
7. The college sector was facing many cost pressures prior to COVID-19 including increased employer contributions to pension schemes and cost of living pay awards. Colleges were focusing on reducing staff costs in order to deliver a balanced budget, having previously delivered significant non-staff cost efficiencies.
8. In 2018-19, the college sector spent £5.5 million on staff restructuring costs in order to reduce costs to a level that would allow them to be financially sustainable in future years. Most of the restructuring was addressed through voluntary severance schemes, however, there were a small number of compulsory redundancies across two colleges.
9. At the end of 2018-19, four colleges (two incorporated and two non-incorporated) reported a net cash outflow from operating activities. However, levels of cash had improved on the previous year with net operating cash inflow as a percentage of total income for the sector at 9%. It is important to note that some of the cash was earmarked for specific purposes, for example, student support and capital maintenance.

Forecast position – Mid-year Returns (MYR) May 2020

COVID-19 has had a significant impact on the financial sustainability of colleges.

10. Colleges were asked to provide mid-year financial forecast information in April, at an early point of lockdown, as part of the regular financial monitoring framework. A revised forecast position was then requested at mid-May, to enable SFC to closely monitor the impact of COVID-19 on the forecast outturn for AY 2019-20. The revised returns highlighted early indications of the significant impact of the COVID-19 outbreak on colleges' financial sustainability. A briefing note, based on the analysis of the forecast position of the university

and college sectors and taking account of the impact of COVID-19, is available on [SFC's website](#).

Updated forecast position - Financial Forecast Return (FFR) June 2020

11. A summary of key college financial indicators across the years 2018-19 to 2022-23 can be found at [Annex A](#). We comment on the key indicators throughout this section of the report.

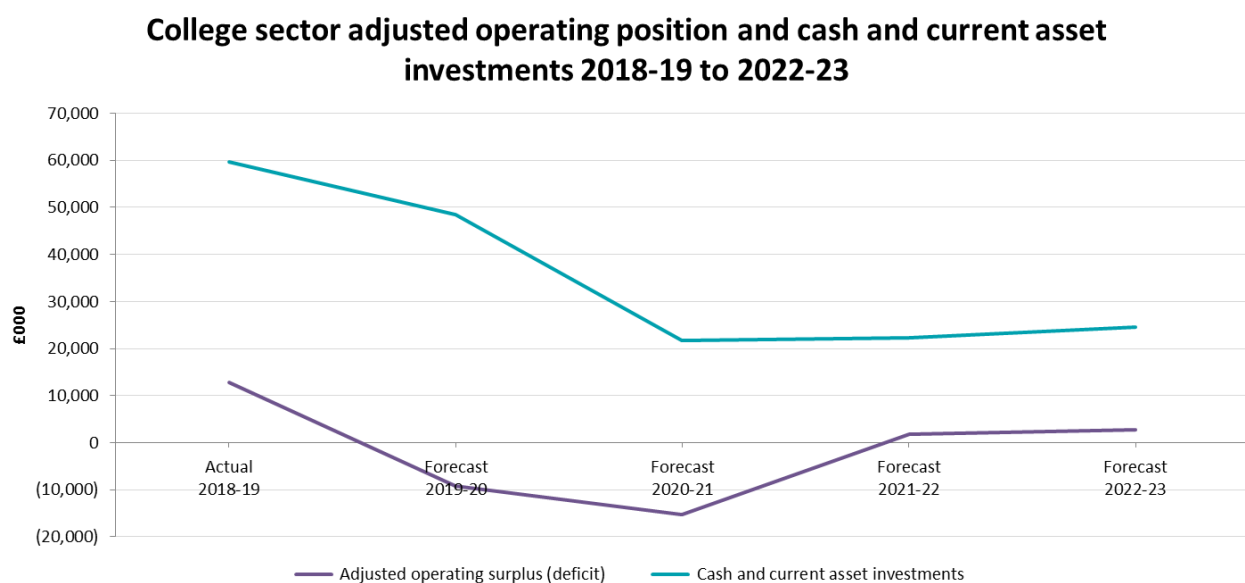
Overall, the college sector's reported future financial position over the next three years is challenging across all indicators of sustainability and it is anticipated that the impact of COVID-19 will be felt most severely in 2020-21.

12. The forecasts collected at the end of June reflect the current impact of COVID-19 and other cost pressures facing the college sector. These other pressures include potential increased employer contributions to Local Government Pension Schemes, funding cost of living pay increases, and estates maintenance. Colleges also face the prospect of reduced European funding unless the impact is offset by the Shared Prosperity Fund.

Adjusted operating position

CJRS income arising from furloughing of staff has been insufficient to offset the projected loss of income.

13. The movement in college sector adjusted operating position and the corresponding movement in cash position from 2018-19 to 2022-23 is shown in the graph below:



14. The sector is forecasting an adjusted operating deficit of £9.2 million in 2019-20. This represents an improvement on the position reported in the updated Mid-Year Return information. The improvement on the operating position is largely due to the inclusion of £6.2 million income from the CJRS and generation of staff and other operating cost savings.

£9M
adjusted operating deficit
(in 2019-20)

15. In aggregate, colleges are forecasting an adjusted operating deficit up to 2020-21, followed by a return to a marginal adjusted operating surplus in 2021-22 reflecting the anticipated lessening impact of COVID-19 and on the planning assumption that restructuring costs are funded by SFC. On the basis of the forecasts submitted, the operational shortfall for 2020-21 is £15.3 million which increases to £20.7 million if there is no SFC funding available for transformation costs.

£15M
adjusted operating deficit
(in 2020-21)

16. There is, however, significant variation between colleges in terms of their financial positions and performance that is not reflected in our aggregate indicators.

Cash and liquidity

Liquidity is clearly going to be a challenge for some colleges over the forecast period.

17. Cash is the most important financial performance indicator and SFC continues to monitor colleges' liquidity closely, particularly in relation to their ability to absorb operational deficits.

18. Sector cash and equivalent balances are expected to reduce by 59% from £59.7 million in 2018-19 to £24.6 million by 2022-23, reflecting the changing operating position. Three colleges are forecasting negative cash balances by the end of July 2023 with one of these colleges failing to show a balanced operating position in the later years of the forecast period. In addition to this, a further five colleges anticipate having less than ten days of cash reserves by the end of July 2023. The significant drop in cash days for the sector over the forecast period can be seen in the graph below:

59% reduction
in sector cash balances

(£60M in 2018-19 to £25M by 2022-23)



3 colleges predict
negative cash balances

(by the end of July 2023)

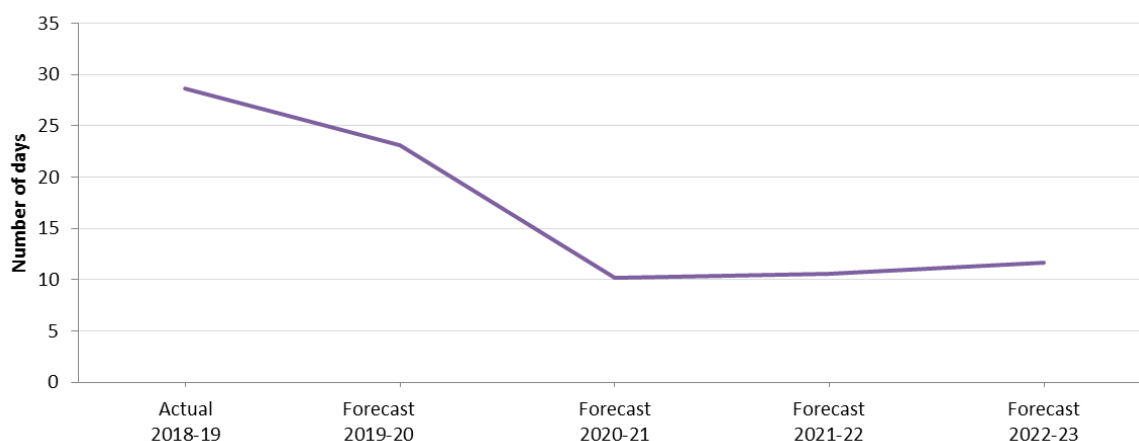


5 colleges predict having
less than 10 days cash
reserves

(by end of July 2023)



**College sector cash as a number of days of expenditure
2018-19 to 2022-23**



19. If SFC transformation funding is unavailable, the levels of cash across the sector will be lower and could result in additional colleges reporting negative cash balances throughout the forecast period.

Net cash inflow from operations

20. At the end of 2018-19, four colleges reported a negative net cash inflow from operating activities. This is forecast to be three colleges by the end of 2022-23. Across all colleges, the net cash inflow from operating activities as a proportion of total income is forecast to move from 8.6% in 2018-19 to 0.7% in 2020-21, increasing again to 4.5% by 2022-23.

Mitigating actions

The route to financial sustainability for many colleges is a reduction in staff costs, including staff restructuring.

21. Staff costs represent the largest element of incorporated college expenditure (68% by the end of the forecast period). They have risen significantly in recent years due to the implementation of national bargaining harmonisation and job evaluation for college staff from April 2017.

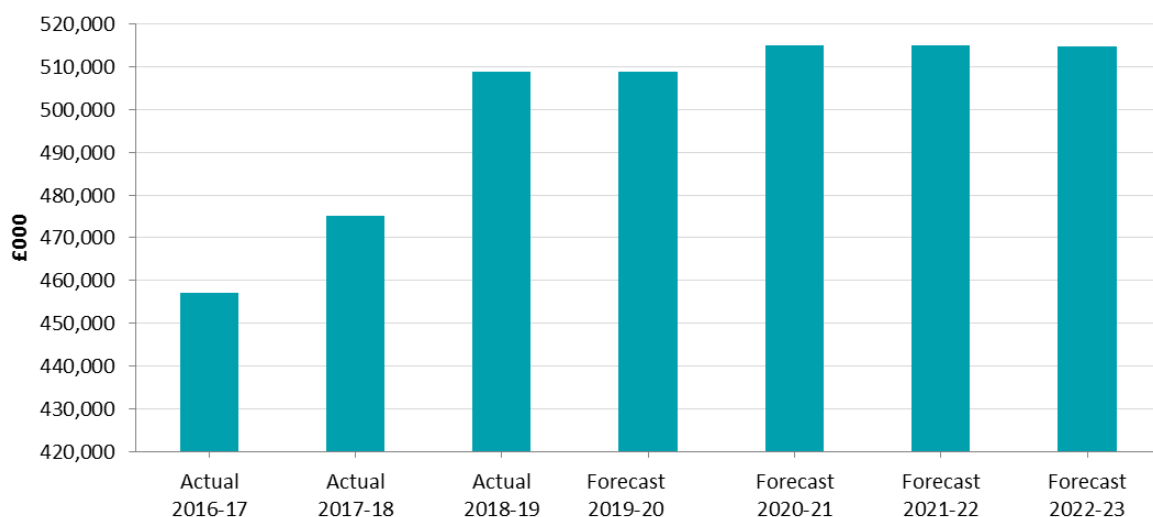
68% of total expenditure
towards staff costs



(expenditure forecast for incorporated colleges)

22. The significant rise in incorporated college staff costs is shown in the graph below:

**Incorporated college staff costs
2016-17 to 2022-23**



23. This is, therefore, an area of focus as further efficiencies will be required in order to deliver a balanced budget, given that the sector has in previous years delivered significant non-staff cost efficiencies. The college sector forecasts indicate that colleges are planning staff restructuring over the forecast period in order to reduce the cost base to levels that allow them to be financially sustainable. Many colleges have also indicated that they expect to generate savings as a result of staff leaving through natural turnover.
24. We recognise that colleges face difficult choices and decisions about their staffing complement, restructuring and cost efficiencies that will need to take into account:
- The resource needed to support economic recovery and deliver SFC activity targets.
 - Any impact on the curriculum offering and their role in providing subject choice in local schools and sustaining local communities, particularly in rural and island areas.
 - The impact on frontline student services and the quality of the student experience.
 - The health and wellbeing of remaining college staff.
 - Their ability to manage backlog maintenance, and sustain estates and learning centres.
25. Other cost savings colleges are considering include:
- Targeting certain categories of discretionary spend.
 - Reducing catering operations.
 - Reviewing curriculum delivery and the introduction of different roles to support the delivery of learning and teaching.
 - Business process re-engineering.

Scenario planning

26. Scenario planning has been undertaken by many colleges. As a result of uncertainties surrounding the impacts of COVID-19 and UK's exit from the EU, colleges will need to review, test and demonstrate their ability to operate on an on-going sustainable basis throughout the period. Given the level of uncertainty and potential material impact, a range of scenarios is likely to be needed and it will be important in each scenario to assess the impact on cash as well as the impact on the operating position.

Key risks

27. In preparing their forecasts, colleges identified a number of risks that could adversely affect their financial performance and sustainability:

- COVID-19 pandemic.
- Changes to the funding model and colleges' ability to deliver regional outcome agreements and Government priorities. This includes the sector's ability to meet the core student activity target of c.116,000 FTE places and other key performance measures.
- The impact of cost efficiencies, including reduced staff numbers and frontline student services, on both the quality of student experience and on the health and wellbeing of college staff, and potentially impacting on colleges' governance requirements.
- The UK's exit from the EU, although this impact could be mitigated by the Shared Prosperity Fund.
- Additional staff costs arising from both cost of living pay awards and the outcome of the National Bargaining job evaluation exercise for support staff.
- Increases in employer contributions to Local Government Pension Schemes.
- Addressing backlog estates maintenance and ICT/digital requirements.
- Challenges of diversifying income and generating additional surplus. The balance of portfolio of provision and how that impacts on student numbers.
- Insufficient funding to meet student support requirements (SFC planning guidance asked colleges to plan on the basis that these costs would be met throughout the planning period).



Financial sustainability of universities

28. At this current time, the financial sustainability of the university sector is extremely fluid, with assumptions being constantly updated as circumstances change.

Key messages

- The COVID-19 pandemic has significantly heightened the challenges facing universities, particularly those with high levels of international and commercial income which has been an important and growing source of income for universities in recent years. Some universities were already experiencing financial challenges (potential increased employer pension contributions, estates costs and UK's exit from the EU), resulting in a weak operating position before they entered the COVID-19 crisis. For those universities the financial challenges have been compounded.
- The Scottish university sector is diverse. While the aggregated underlying financial position in 2018-19 shows the sector overall to be in good financial health, it masks significant variation. Surpluses are concentrated in three of the four ancient universities.
- The university sector's future financial position is challenging across all indicators of sustainability, and for 2020-21 in particular. While forecasts for 2019-20 and 2020-21 have improved on the returns provided at the end of April, a substantial deficit is still projected for 2020-21. Most institutions have identified mitigating actions which only include staff restructuring activity in the most pessimistic scenarios.
- Institutions' financial positions should become clearer in late autumn when student numbers are confirmed.
- Cash and cash generation are the most important financial performance indicators and short-term liquidity remains universities' main challenge.
- There is a risk that universities with large amounts of external borrowing, in the form of private placements, are unable to build up sufficient cash reserves in order to make the repayments required at set points in time over the term of the borrowing.
- The impact of COVID-19 will be seen for years to come and, due to increased international competition, the sector may never recover to the 2018-19 levels of international student recruitment.

Actions to date

Emergency response for 2019-20 & 2020-21

- **Additional support for research:** The Scottish Government announced a one-off £75 million package of support for research for AY 2020-21 which recognises the importance of Scotland's university research base to the nation's future prosperity and wellbeing, as well as to its international reputation.
- **Targets:** We confirmed that we would not recover funds for shortfalls against outcome agreement targets (including funded student places) where these are related to COVID-19 for AY 2019-20. We subsequently confirmed the same position for AY 2020-21. For institutions delivering controlled subjects, we agreed to work with Scottish Government departments on the potential recovery of funds.
- **Reporting requirements:** SFC engaged rapidly with institutions to provide reassurances that we would keep returns and reporting requirements to a minimum, focusing on absolute priorities to ensure continued compliance with legislative requirements.
- **Additional capital announcements:** In August, SFC announced £2.4 million of additional capital funding for universities in FY 2020-21 to support the provision of ICT equipment for learners to help tackle digital poverty. In addition, SFC announced £3.5 million of additional capital funding to support the economic recovery in FY 2020-21.
- **Student places:** Additional funded student places will be allocated to universities in AY 2020-21 following the Scottish Qualifications Authority (SQA) results. It should be noted that the impact of these additional funded places are not reflected in any of the forecasts captured in this report.
- **Coronavirus Job Retention Scheme (CJRS):** Universities were eligible to apply to the UK Government scheme. CJRS funding is included in the forecasts captured in this report.
- **UKRI-costed grant extensions:** On 27 June, UKRI [announced](#) an award of £150 million to UK universities to allow for the additional (largely staff) costs of resuming COVID-interrupted research grants. Individual allocations by UKRI to universities were calculated based on the value of the UKRI grants held by an organisation whose funding finishes between 1 April 2020 and 31 March 2021. It should be noted that the impact of this funding is not reflected in the forecasts captured in this report.
- **World Class Labs:** The UK R&D [Roadmap](#) contained an announcement of

£300 million to upgrade scientific infrastructure across the UK through the UK Government's World Class Labs funding scheme. This will be delivered through a variety of mechanisms, with around £10 million expected to pass through SFC in increased research capital for universities. It should be noted that the impact of this funding is not reflected in the forecasts captured in this report.

- **UK Government Research Stabilisation package:** The package, announced on 27 June, is expected to compensate for 80% of international student fee losses, capped at each university's non-public research income. The package of 75% loan and 25% grant will be available before the end of FY 2020-21. It should be noted that the impact of this funding is not reflected in the forecasts captured in this report.

Medium to long-term actions

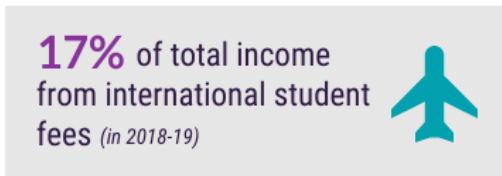
- We are undertaking a review of coherent provision and [sustainability](#).
- We are reassessing our regulatory, data and reporting requirements.

Annual Accounts 2018-19 (baseline year)

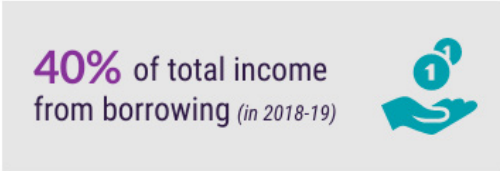
29. A full analysis of the 2018-19 financial position of the college and university sectors, as shown in the financial statements, can be found on [SFC's website](#). This analysis presents an aggregate picture of the financial health of Scottish institutions based on a review of the 2018-19 financial statements of the 18² higher education institutions. While the analysis presents an aggregate position, there is significant variation in the financial position of individual universities. This analysis highlights the main issues that the university sector was dealing with prior to the impact of COVID-19.

30. The analysis highlights that in the 2018-19 annual accounts, the sector's underlying operating position appears fairly positive, with a surplus of £96.4 million. This was an improvement on the previous year's underlying operating position. However, despite the positive sector position, nine of the 18 universities reported underlying operating deficits in 2018-19, in line with the previous year's result.

31. The analysis also highlights the significance of international student fees as a source of income for universities. In 2018-19, they accounted for 17% of total income. Many universities had forecast quite ambitious targets for 2018-19 and exceeded those targets. However, five universities did not meet their planned levels in 2018-19. One institution forecast a reduction in this income stream in 2018-19 and did not meet the reduced target. It is clear that universities need this source of income in order to remain financially sustainable and to support other areas of their operations e.g. research is a loss making activity and it is therefore important that universities address this through other surplus generating activity.



32. In 2018-19, the sector reported good liquidity but borrowing was at its highest recorded level for the sector, representing 40% of total sector income. Average borrowing for the sector was 33% of total income with ten universities reporting above average borrowing. Building up cash reserves, through



generating ongoing surpluses, is vital to allow universities with Private Placement borrowing to repay large bullet payments at the set points over the term of the borrowing.

² The Open University in Scotland is not included in this analysis due to different reporting arrangements in place.

Forecast position - Financial Forecast Update April 2020

It is clear that the impact of the COVID-19 outbreak on universities' financial sustainability is extremely significant particularly for ancient and chartered universities in 2020-21.

33. Universities were asked to provide a Financial Forecast Update (FFU) for Academic Years 2019-20 and 2020-21 by 24 April 2020. This return was required to identify financial impacts arising from the COVID-19 emergency. The return also enabled universities to demonstrate how they were working to mitigate financial impacts, including the reprioritisation of existing resources and deferral of expenditure, as well as the development of additional planning scenarios.
34. A briefing note, based on the analysis of the forecast position of the university and college sectors, taking account of the impact of COVID-19, is available on [SFC's website](#).
35. As stated in the analysis of the 2018-19 annual accounts, the university sector is heavily reliant on international student fee income and this income has been essential to cross subsidise other activities (e.g. research). Reductions on the basis of the assumptions included in SFC planning guidance (50% reduction on international student new intakes and a reduction of 30% on international students continuing studies) would have a substantial financial impact.
36. The briefing note highlights the forecast deterioration in the operating deficit position under the assumptions set out in the SFC guidance and referred to in the paragraph above.

Updated forecast position - Strategic Plan Forecast (SPF) July 2020

37. A summary of key university financial indicators, by type of institution, across the years 2018-19 to 2020-21 can be found at [Annex B](#). We comment on the key indicators throughout this section of the report.

The impact of COVID-19 will be seen for years to come and, due to increased international competition, the level of international student recruitment will remain a key risk for the sector.

38. The forecasts sent to SFC at the end of July provide an update on the position reported in the FFU returns collected at the end of April and reflect the impact, at that point in time, of COVID-19 and other cost pressures facing the university sector. It is clear from the financial returns that the sector's future financial

position remains challenging across all indicators of sustainability, and for 2020-21 in particular. Universities have indicated that the impact of COVID-19 will be seen for years to come. Universities' financial positions should become clearer following the confirmation of student recruitment numbers in late autumn.

Impact of COVID-19

39. The main financial impacts include lower income from the following funding streams: Fee income (overseas, RUK and short-course provision); income from residences, catering and sport; and donations and endowments as a result of stock market falls.
40. The majority of universities' costs are staff costs of which a small amount is offset by income from the CJRS. Institutions are also incurring additional costs in the following areas:
 - IT and support costs to support online teaching, and assessment and feedback.
 - Contract costs associated with the suspension of work on campus redevelopment.
 - Refunding students who left university accommodation early at the start of lockdown.
 - Reimbursement of cancelled travel.
 - Repatriating Erasmus students.
 - The purchase of Personal Protective Equipment (PPE) for students and staff, hand sanitiser dispensers and signage necessary for the return of students and staff to the campus.
41. Savings are expected in the following areas: academic materials and consumables; utilities; property costs; photocopying; and travel and subsistence. More detail can be found in the section on mitigating actions below.

Underlying operating position

42. In aggregate, universities are forecasting an underlying operating surplus in 2019-20 of £46.4 million and a deficit of £176.1 million in 2020-21.

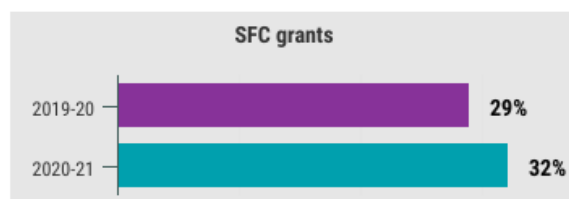


This represents an improvement on the position reported in the April FFU returns.

43. The improved underlying operating position takes account of CJRS income as well as an additional £75 million SFC research funding and City Deal funding which may not have matching expenditure in the forecast period. Several universities have also revised upwards levels of international fee income projections on the basis of latest recruitment data while many institutions have factored additional staffing and other operating cost efficiencies into their latest forecasts. While the latest forecasts represent an improvement on the FFU projections, the 2020-21 position will not become clear until late autumn when student recruitment numbers are confirmed.
44. Also, there are cost pressures that need to be considered e.g. employer pension contributions, which have increased substantially in recent years and will continue to rise placing more pressure on the financial sustainability of universities. In addition, the cost of maintaining buildings represents a significant pressure on university budgets.

Reliance on SFC grant

45. SFC grants are projected to account for 29% of total sector income in 2019-20, increasing to 32% in 2020-21. This reflects the impact of COVID-19 on the university sector's ability to generate income from international student fees and other non-government income in 2019-20 and 2020-21.

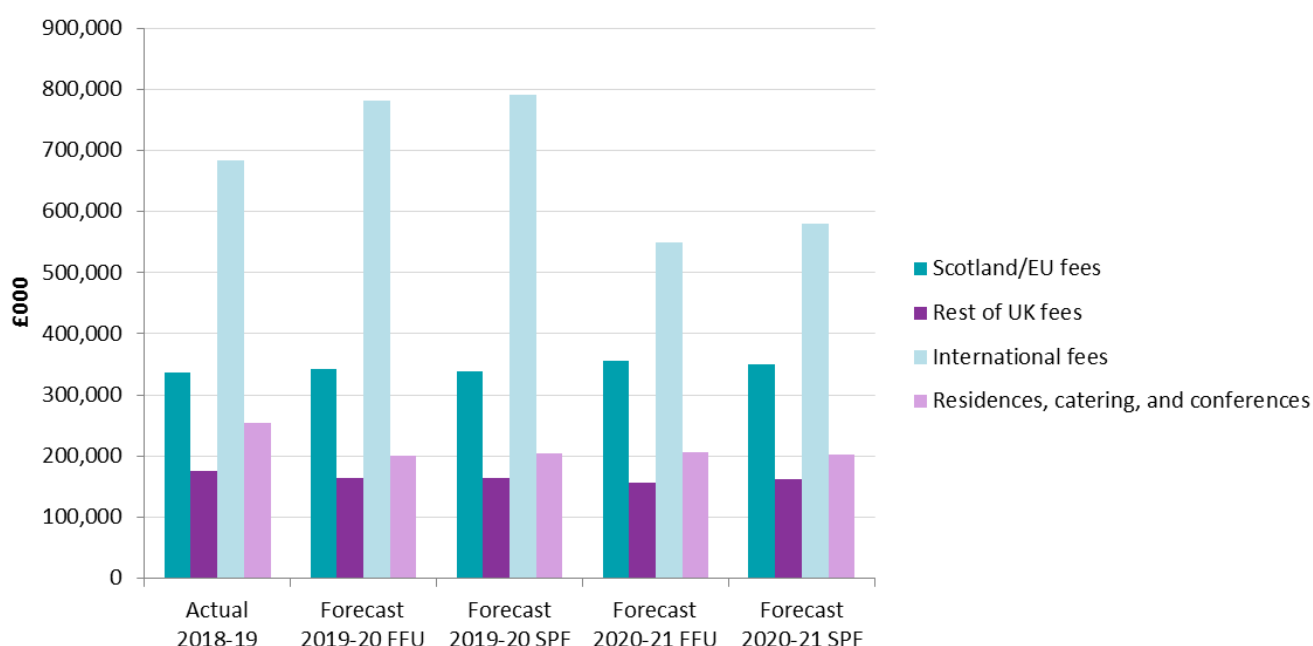


Other sources of income (non-SFC)

The COVID-19 pandemic has heightened the challenges facing universities particularly those with high levels of international and commercial income which has been an important and growing source of income for universities in recent years.

46. International fee income is expected to increase from 2018-19 levels (£684.2 million) to £790 million in 2019-20 (FFU: £782.2 million) before falling to £578.6 million in 2020-21 (FFU: £548.6 million).
47. While rest of UK (rUK) student fee income is expected to fall from £175.7 million in 2018-19 to £162.4 million in 2020-21 (FFU: £156.9 million), Scotland/EU fee income is expected to increase from £336.8 million to £350.3 million (FFU: £356.7 million) over the same period.

48. Income from residences, catering and conferences is projected to reduce from £253.8 million in 2018-19 to £204.4 million in 2019-20 (FFU: £201.6 million) with a further reduction to £202.6 million in 2020-21 (FFU: £207.0 million).

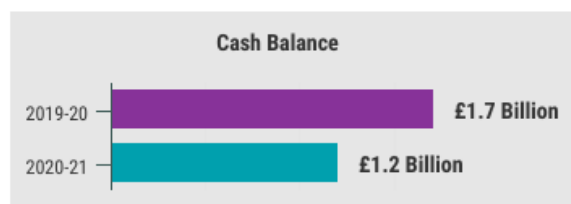


49. All of the other sources of income come with associated costs and some of the activities can be loss making e.g. research. This was highlighted in SFC’s report [Financial Sustainability of Colleges and Universities in Scotland](#).

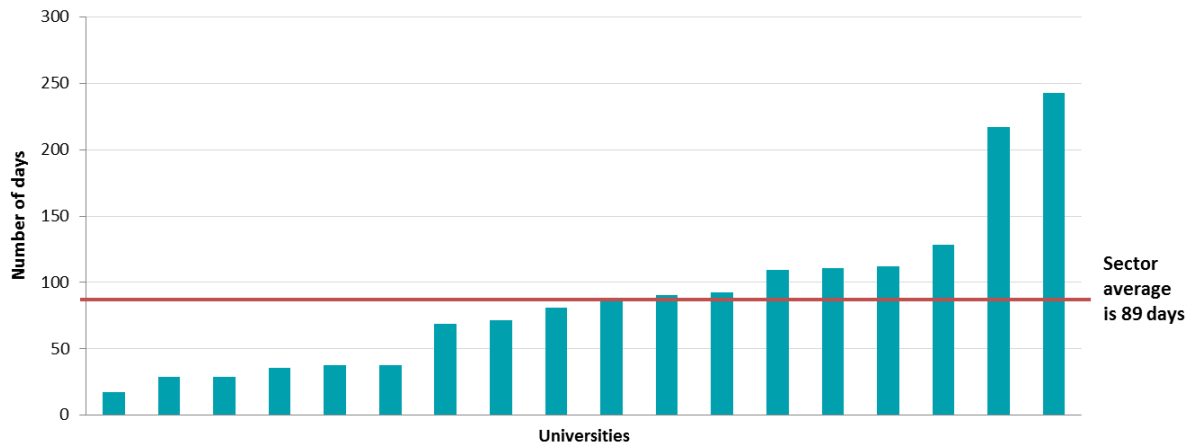
Cash and liquidity

Cash and cash generation are the most important financial performance indicators and short-term liquidity remains universities’ main challenge.

50. Sector cash and equivalent balances are expected to increase from £1.183 billion in 2018-19 to £1.700 billion in 2019-20 before reducing to £1.228 billion by 2020-21. The 2019-20 and 2020-21 balances are improved on the FFU position as a result of the improved operating position. No university is forecasting a negative cash balance by the end of July 2021, however, six universities anticipate having less than two months of cash reserves by the end of July 2021 as highlighted in the chart below.



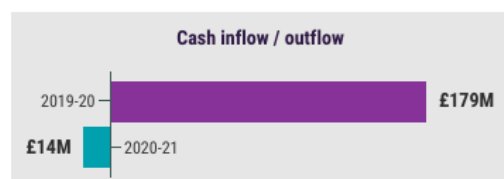
University sector cash shown as a number of days of expenditure forecast for 2020-21



- 51. The focus for many universities during the COVID-19 pandemic is therefore on protecting their cash position and thereby their ability to absorb short-term operational deficits.
- 52. It is important to note that, when considering sector cash balances, they may be artificially inflated by unspent funds, for example, unspent borrowing for capital projects. Universities will have borrowed for different purposes. For some, their borrowing will be tied to their capital programme and therefore this borrowing cannot be used to sustain operations. That is a condition of borrowing with some lenders. So the cash position of universities needs to be set in the context of their inability to vire cash to sustain their operations without their lender’s permission.

Net cash inflow from operations

- 53. Across all universities, the net cash inflow from operating activities is forecast to reduce from an inflow of £178.6 million in 2019-20 (4.4% of overall income) to an outflow of £13.9 million in 2020-21 (-0.3% of total income. Three universities anticipate a net cash outflow from operating activities during 2019-20 which is forecast to increase to nine universities in 2020-21.

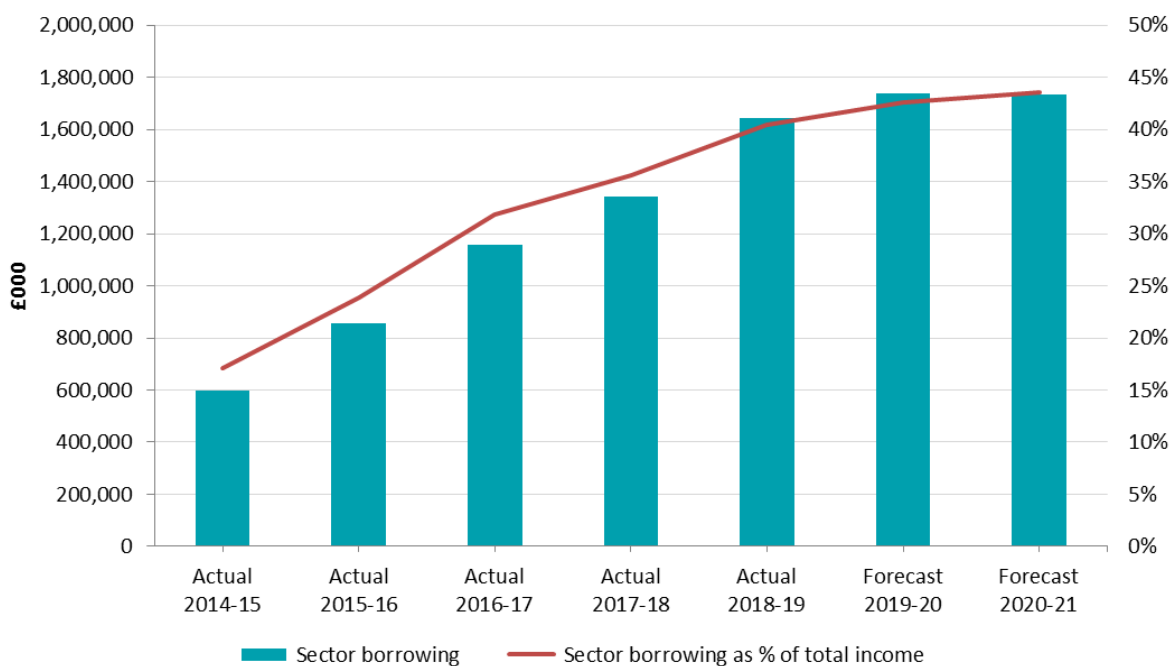


Borrowing

There is a risk that universities with large amounts of borrowing are unable to build up sufficient cash reserves in order to make the repayments required at set points in time over the term of the borrowing.

54. Universities' total long-term borrowing is forecast to increase from £1.645 billion at the end of 2018-19 to £1.735 billion at the end of 2020-21. The graph below shows the increase in sector borrowing from 2014-15 through to 2020-21 which reflects the investment that universities have made in their estates over this period:

University sector borrowing and borrowing as % of total income 2014-15 to 2020-21



55. Forecast borrowing as a percentage of total income is expected to increase from 40% in 2018-19 to 44% in 2020-21. Capital expenditure of £1.249 billion is projected over the planning period.
56. Short-term liquidity is universities' main challenge and several universities have agreed overdraft or revolving credit facilities with lenders to help them manage through the crisis. Some have also been exploring accessing UK Government Loan Schemes, however, no borrowing from this source has been reported in the latest forecasts.

View of lenders

57. SFC has recently been engaging with banks on the issue of covenants attached to borrowing and the universities have included some information on this in their most recent forecasts.
58. No banking covenants were breached during 2019-20, however, several universities have indicated that they may breach lenders' covenants in 2020-21 although the position will not become clear until late autumn when student numbers are confirmed. Universities are engaging on a regular basis with lenders and keeping them fully apprised.
59. Lenders appear supportive, are taking a pragmatic approach and have indicated a willingness to renegotiate covenants where breaches are related to COVID-19. While some universities have already amended existing covenants with lenders to allow the required level of short-term finance, it is likely that the bulk of the work on covenant revisions will be put on hold pending confirmation of 2020-21 student recruitment levels.
60. Private Placement lenders, similar to banks, are awaiting updates on student recruitment levels later this year but have been keen to understand that interest payments will be maintained in gaining assurance around universities' trajectory back to sustainability.

Mitigating actions

61. Most universities have set out actions to mitigate deficits which do not include staff restructuring activity in the first instance. Given ongoing uncertainties about 2020-21 levels of student recruitment, it is essential that institutions remain flexible enough to respond to future opportunities without a depleted workforce. Staff restructuring, including compulsory redundancies, can therefore be seen as a mitigating action in the most pessimistic of scenarios provided. Many universities have also indicated that they expect to generate staff savings as a result of a freeze on vacant posts, placing in-progress posts on hold, keeping pay awards to a minimum and staff leaving through natural wastage. Additional income has been generated by universities by taking advantage of the CJRS.
62. Other non-staff costs mitigations include:
 - Freezing non-essential spend.
 - Delaying or not continuing capital projects unless legally committed.
 - Reduced operating expenses – lower catering, utilities and maintenance.

- Reduced research expenditure due to some laboratories being closed during the lockdown period.
 - Consolidation of activity within the current university estate.
 - Deferring start dates for specific courses to January.
 - Taking advantage of VAT payment deferral schemes.
 - Re-negotiating payment plans with suppliers.
63. Again, it is important that universities balance the need to take mitigating actions with their ability to recover and compete successfully in future years.
64. Universities will need to balance the need to restructure with their requirement to deliver outcomes and Government priorities, in particular the ability to support economic recovery and meet student targets. We expect universities to respond to financial challenges in ways that sustain and prioritise delivery of good quality teaching and learning for students and enhance the overall student experience and wellbeing of the university workforce.
65. Universities are continuing to monitor student acceptances very closely and levels of applications have been encouraging to date. It is possible that lack of employment opportunities may encourage prospective students to look positively towards higher education. Conversely, the additional costs and borrowing required to support students during their studies may be seen as challenging during a period of recession.

Scenario planning

66. Universities have chosen to use various scenarios in their forecasts ranging from pessimistic to aspirational positions. Some universities have provided SFC with two or three scenarios, demonstrating that their governing body is looking at a range of information in their deliberations on the future sustainability of the university.

Key risks

67. There are a number of risks that could adversely affect universities' financial performance and sustainability. The most significant risk areas for universities relate to:
- Impact of COVID-19 pandemic and the potential consequential failure to achieve international student recruitment targets.
 - The UK's exit from the EU, although this impact could be mitigated by the Shared Prosperity Fund and the nature of the future relationship between

the UK and the EU in terms of research and mobility.

- Rise in staff and pension costs.
- Fall in RUK recruitment in an increasingly competitive market.
- The UK Government's response to the Review of Post-18 Education and Funding in England, as lower tuition fees in England could have a significant impact on Scottish institutions, and other education policies that may affect Scottish institutions.
- UK visa and immigration regulations.
- Further unanticipated public spending cuts in teaching and/or research income.
- Impact of changes to UK research funding in the Higher Education and Research Act 2017.
- Failure to effectively manage major capital investment programmes and their financial impacts.

Key financial indicators for the college sector	Annual accounts	Revised	FFR	FFR	FFR	FFR
	2018-19	MYR 2019-20	2019-20	2020-21	2021-22	2022-23
Total income (£000)	773,972	759,828	762,447	776,291	776,176	776,596
SFC grant as % of total income	76%	74%	77%	79%	78%	77%
Operating surplus/(deficit) (£000)	(46,426)	(26,862)	(23,701)	(26,699)	(11,082)	(10,789)
Operating surplus/(deficit) as % of total income	(6.0%)	(3.5%)	(3.1%)	(3.4%)	(1.4%)	(1.4%)
Adjusted operating surplus/(deficit) (£000)	12,887	(12,342)	(9,191)	(15,322)	1,774	2,700
Adjusted operating surplus/(deficit) as % of total income	1.7%	(1.6%)	(1.2%)	(2.0%)	0.2%	0.3%
Cash and current asset investments less overdrafts (£000)	59,711	40,885	48,472	21,801	22,241	24,637
Cash days	29	21	23	10	11	12
Net operating cashflow (£000)	66,904	12,600	28,315	5,174	34,483	35,235
Net operating cashflow as % of total income	8.6%	1.7%	3.7%	0.7%	4.4%	4.5%
Total borrowing (£000)	266,047	263,672	255,229	244,561	233,607	222,345
Total borrowing as % of total income	34%	35%	33%	32%	30%	29%

Key financial indicators by type of university	HESA FSR Annual Accounts Actual 2018-19	FFU		SPF	
		2019-20	2020-21	2019-20	2020-21
Ancient	2,275,342	2,254,767	2,166,410	2,304,214	2,211,475
Chartered	955,919	954,869	924,121	956,814	975,312
Modern	679,422	675,974	656,935	673,421	663,366
SSI	157,970	144,975	135,674	145,755	134,853
Total income (£000)	4,068,653	4,030,585	3,883,140	4,080,204	3,985,006
Ancient	21%	21%	22%	21%	24%
Chartered	30%	29%	30%	29%	31%
Modern	57%	57%	60%	58%	61%
SSI	34%	37%	40%	38%	42%
Funding Council grant as % of total income	30%	29%	31%	29%	32%
Ancient	(275,167)	128,711	(195,621)	326,032	(110,711)
Chartered	(184,026)	70,844	(109,330)	93,030	(38,192)
Modern	(41,520)	(29,031)	(65,081)	(14,185)	(34,007)
SSI	(1,958)	(4,060)	(13,423)	(3,544)	(8,270)
Operating surplus/(deficit) (£000)	(502,671)	166,464	(383,455)	401,333	(191,180)
Ancient	(12.1%)	5.7%	(9.0%)	14.1%	(5.0%)
Chartered	(19.3%)	7.4%	(11.8%)	9.7%	(4.0%)
Modern	(6.1%)	(4.3%)	(9.9%)	(2.1%)	(5.1%)
SSI	(1.2%)	(2.8%)	(9.9%)	(2.4%)	(6.1%)
Operating surplus/(deficit) as % of total income	(12.4%)	4.1%	(9.9%)	9.8%	(4.8%)
Ancient	109,716	32,324	(195,621)	67,856	(110,712)
Chartered	(1,400)	(16,856)	(109,340)	(12,820)	(29,124)
Modern	(26,255)	(20,483)	(63,517)	(7,254)	(29,026)
SSI	14,321	(1,960)	(12,223)	(1,390)	(7,270)
Operating surplus/(deficit) adjusted for staff restructuring costs and pension revaluation (£000)	96,382	(6,975)	(380,700)	46,392	(176,132)
Ancient	4.8%	1.4%	(9.0%)	2.9%	(5.0%)
Chartered	(0.1%)	(1.8%)	(11.8%)	(1.3%)	(3.0%)
Modern	(3.9%)	(3.0%)	(9.7%)	(1.1%)	(4.4%)
SSI	9.1%	(1.4%)	(9.0%)	(1.0%)	(5.4%)
Operating surplus/(deficit) adjusted for staff restructuring costs and pension revaluation as % of total income	2.4%	(0.2%)	(9.8%)	1.1%	(4.4%)

Key financial indicators by type of university	HESA FSR Annual Accounts Actual 2018-19	FFU 2019-20	FFU 2020-21	SPF 2019-20	SPF 2020-21
	Ancient	749,420	1,097,776	614,280	1,238,971
Chartered	268,531	259,607	156,440	266,567	198,441
Modern	122,138	110,370	71,944	148,357	122,220
SSI	42,421	45,264	34,368	46,412	38,465
Cash and current asset investments less overdrafts (£000)	1,182,510	1,513,017	877,032	1,700,307	1,228,157
Ancient	113	201	102	245	146
Chartered	92	116	59	122	77
Modern	66	61	39	84	68
SSI	104	118	89	121	105
Cash days	100	153	80	181	115
Ancient	176,799	56,986	(90,748)	106,582	(36,918)
Chartered	58,837	29,558	(45,795)	38,751	17,313
Modern	44,764	19,294	(12,348)	33,941	8,349
SSI	8,258	1,053	(7,984)	(710)	(2,638)
Net cash flow from operating activities (£000)	288,658	106,891	(156,875)	178,564	(13,894)
Ancient	7.8%	2.5%	(4.2%)	4.6%	(1.7%)
Chartered	6.1%	3.1%	(5.0%)	4.0%	1.8%
Modern	6.6%	2.9%	(1.9%)	5.0%	1.3%
SSI	5.2%	0.7%	(5.9%)	(0.5%)	(2.0%)
Net cash flow from operating activities as % of total income	7.1%	2.7%	(4.0%)	4.4%	(0.3%)
Ancient	1,098,852	1,126,160	1,118,791	1,126,161	1,116,216
Chartered	292,842	346,574	380,931	347,430	360,581
Modern	245,333	257,096	251,515	256,333	249,330
SSI	8,642	9,837	8,875	9,837	8,874
Total borrowing (£000)	1,645,669	1,739,667	1,760,112	1,739,761	1,735,001
Ancient	48%	50%	52%	49%	50%
Chartered	31%	36%	41%	36%	37%
Modern	36%	38%	38%	38%	38%
SSI	5%	7%	7%	7%	7%
Total borrowing as % of total income	40%	43%	45%	43%	44%