Summary financial position of the university sector: Analysis of 2017-18 financial statements

Summary

A total of eighteen institutions submitted financial statements for the year ending 31 July 2018. Overall the sector is in reasonable financial health based on the review of the 2017-18 financial statements, however, this position varies on an individual institutional basis.

The introduction of the FRS 102 accounting standard in 2015-16 resulted in greater volatility in the annual operating position of institutions which makes it more difficult to look at trends in operating position over the years. This is mainly due to a mismatch between reporting of income and related expenses, particularly in relation to capital grants received by institutions.

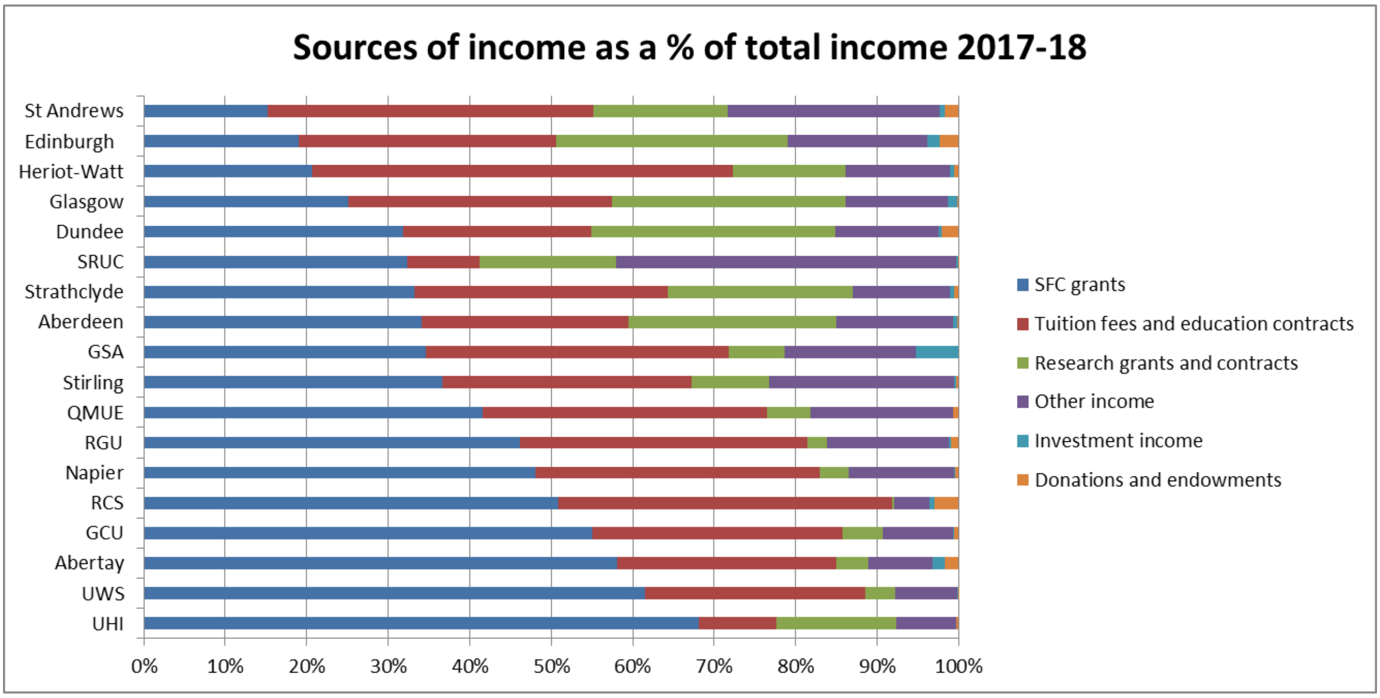
The sector continues to face uncertainties including the UK's exit from the EU, and significant cost pressures including increases in employers' contributions for pension schemes and general inflation. In light of the uncertain environment they now operate in, institutions need to ensure that their financial planning includes adequate contingency measures. A list of key risks is included at the end of this paper.

Summary of key financial indicators

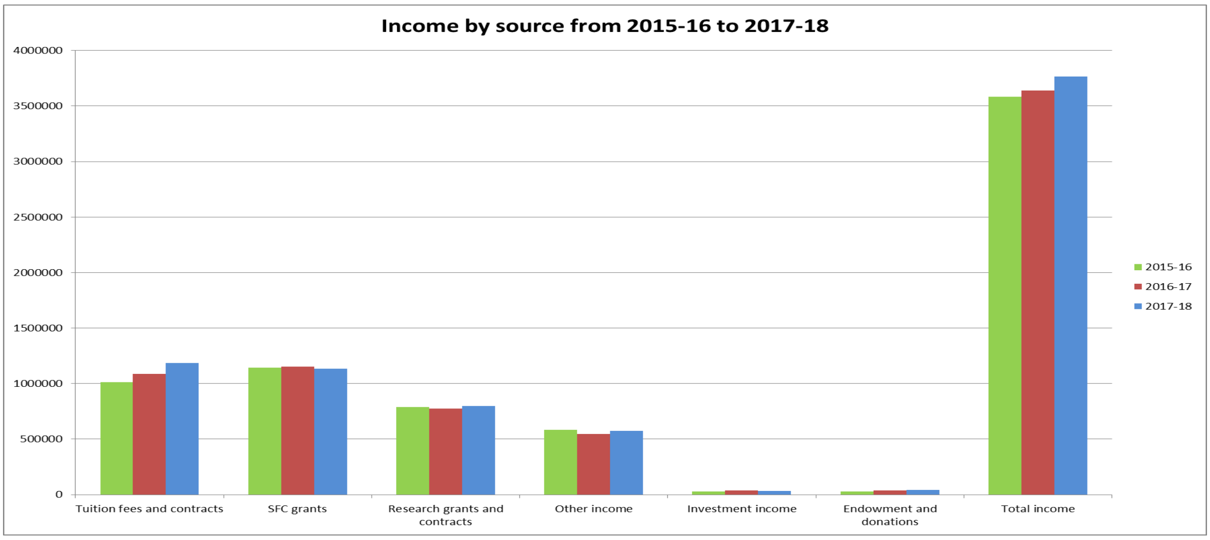
Key financial performance indicators	Actual 2017-18 £000	Actual 2016-17 £000
Total income	3,765,359	3,636,970
SFC grant as a % of total income	30%	32%
Operating surplus/(deficit)	(2,125)	79,729
Operating surplus/(deficit) as a % of total income	(0.1%)	2.2%
Net operating cash flow	252,916	271,599
Net operating cash flow as a % of total income	7%	7%
Cash and cash equivalents net of overdrafts	1,152,546	1,226,812
Cash days	119	135
Borrowing	1,342,559	1,158,772
Borrowing as a % of total income	36%	32%

Income

Overall sector income increased by 3.5% in 2017-18. The sector receives 30% of its income from the Scottish Funding Council (SFC). The graph below provides a view of sources of income as a percentage of total income by institution and shows that the amount of SFC funding varies widely on an institutional basis:



The graph below shows that tuition fees and education contracts have taken over as the main source of income for the sector in 2017-18 although this is not the case for all institutions.



Operating position

Overall, the university sector's operating position for the year ending 31 July 2018 is a deficit of £2.1 million compared to a prior year surplus of £79.7 million. The major movements in operating surplus on a sector basis are outlined below:

Movement in year	£ million
Increase in sector income	128
Increase in staff costs	(77)
Increase in other operating costs	(79)
Increase in restructuring costs	(27)
Other (depreciation, interest)	(27)
Net decrease in surplus	**(82)**

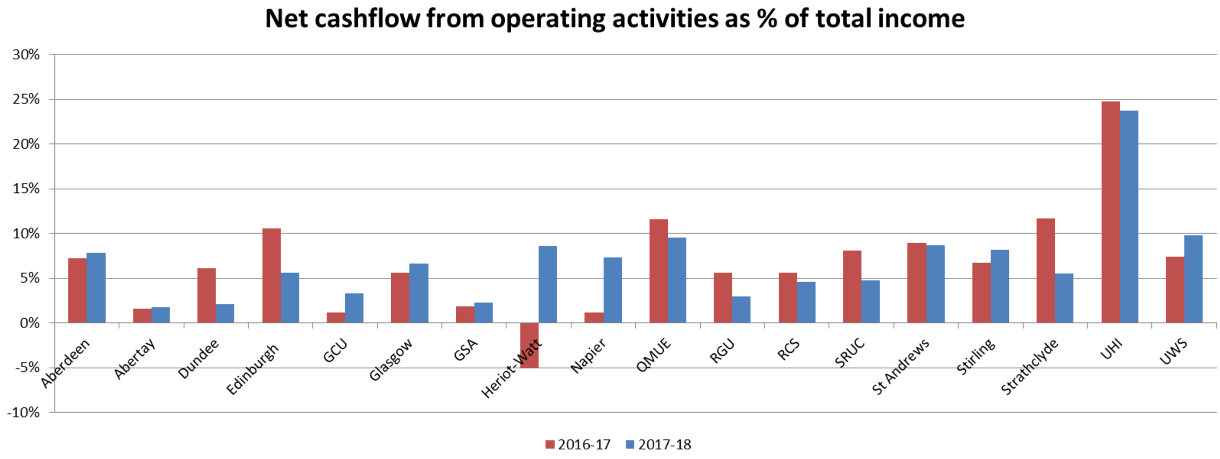
There are significant variations in individual institution results. Ten of the eighteen institutions reported an operating deficit totalling £81.3 million and eight institutions reported an operating surplus totalling £79.2 million.

Again, it is important to note that the implementation of the FRS 102 accounting standard in 2015-16 has distorted the operating position by introducing more volatility through various accounting adjustments. There may therefore be a mismatch between reporting of income and related expenditure particularly in relation to capital grants received by institutions.

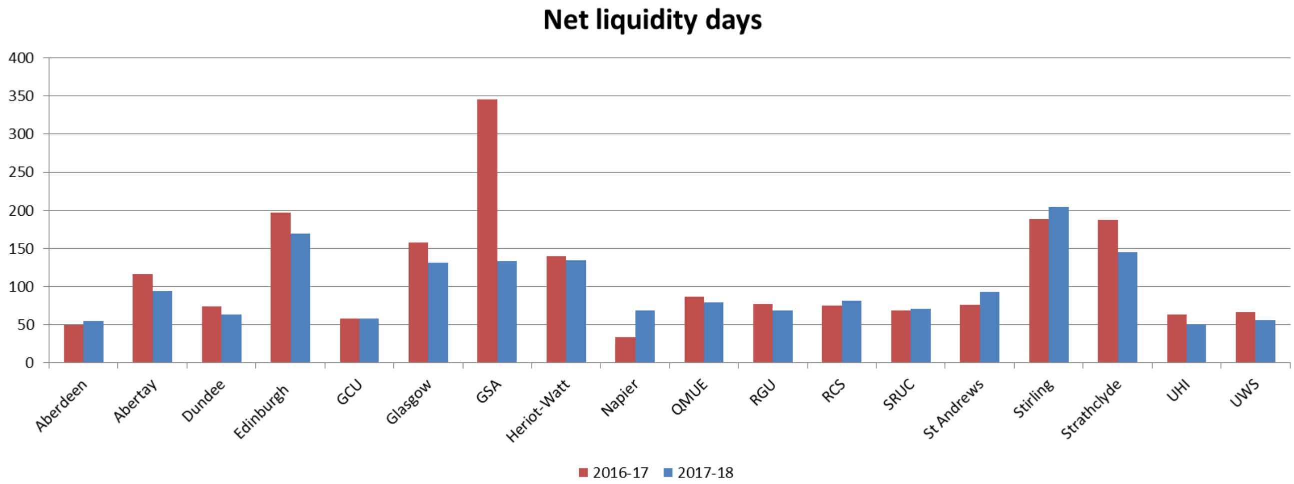
Balance sheet performance

University sector cash and short-term investments amounted to £1,153 million at the end of 2017-18, a decrease of £74 million from last year.

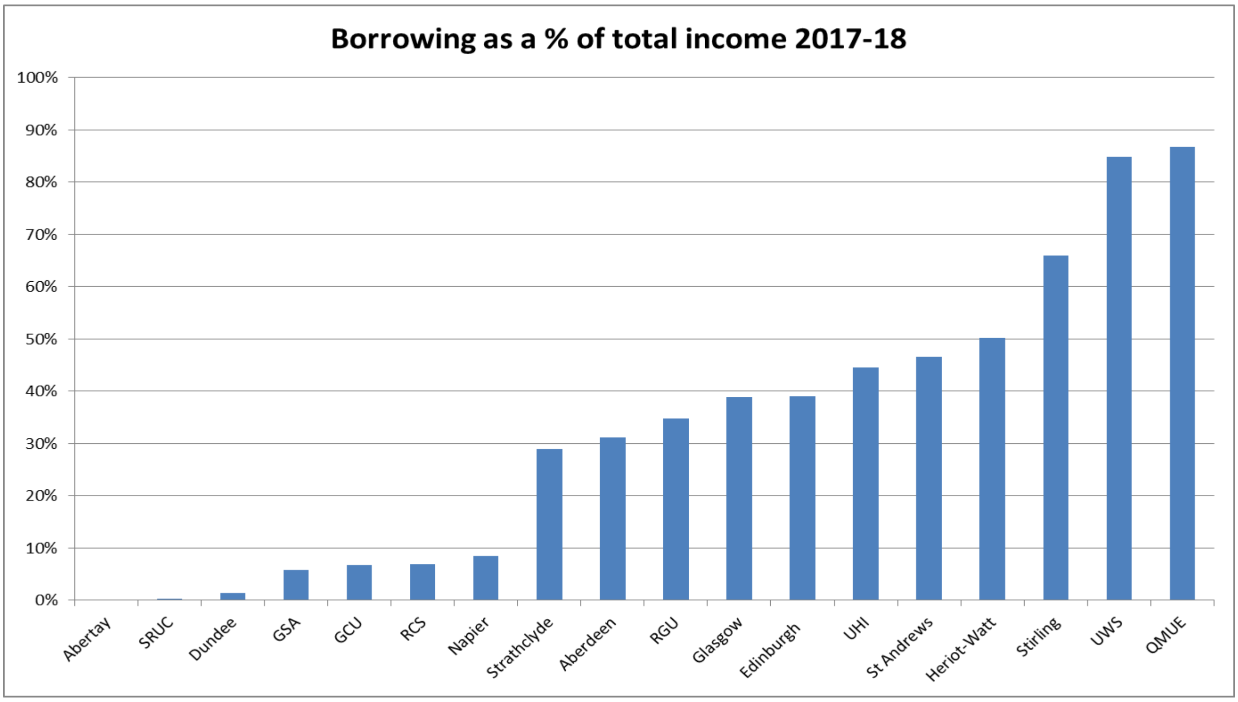
During 2017-18, the sector reported a net cash inflow from operating activities (surplus for the year adjusted for non-cash items and financing/investing activities) of £253 million. Details of institutions' net cash inflow from operating activities as a percentage of total income are set out in the graph below.



In 2017-18, net liquidity days varied from 51 to 205 and six institutions are holding sufficient cash reserves to cover over 100 days of expenditure. Details of institutions' net liquidity days are provided in the graph below.



External borrowing has increased in 2017-18 by £177 million to reach £1,336 million. The main reason for this increase is a small number of institutions having significant programmes of capital expenditure which are being financed in part through borrowing. Two institutions have no external borrowings. For the others, borrowing ranges from 1% to 87% of total income with an overall average of 33%. Details of institutional borrowing as a percentage of total income are set out in the graph below.



There is an increased use of private placements as a form of borrowing by institutions which involves large bullet capital payments at set points in the future. Out of the total borrowing figure of £1,336 million, £574 million is in the form of private placements. Institutions with this type of borrowing will have to ensure that cash is available to repay the borrowing in the years specified.

Institutions paid £34.5 million in loan interest in 2017-18, an increase on 2016-17 (£29.7 million), reflecting the additional borrowing.

Key risks to financial sustainability

There are a number of risks that could adversely affect the financial performance and sustainability of institutions and the negative consequence of this could be a reduction in areas of activity which are important for the Scottish economy e.g. research activity. The most significant risk areas for institutions relate to:

- Impact of the UK exiting from the European Union.
- Rise in staff costs and employer pension contributions arising from recent valuation exercises.
- Failure to achieve international student recruitment targets.
- Fall in Rest-of-UK recruitment in an increasingly competitive market.
- UK Visa and Immigration regulations and requirements.

- Unanticipated public spending cuts in research and/or teaching 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, and estates maintenance backlog.

- Review of Post-18 Education and Funding in England – lower tuition fees could have a significant impact on Scottish universities.