University Sector Private Placement Borrowing

Purpose

1. The purpose of this paper is to **consider** universities' arrangements for the repayment and monitoring of their Private Placement borrowing.

Recommendation

2. To consider the update based on an analysis of questionnaires recently returned by institutions.

Financial implications

3. There are no specific programme fund or running cost implications arising from this paper that are not already allowed for in the Council's programme fund or running cost budgets.

Risk assessment

4. There is a risk that institutions with borrowing in the form of Private Placements will have insufficient funds to make the large bullet repayments at the set points, albeit the earliest loan repayment is not until 2027. This risk is mitigated through establishment of loan servicing funds by institutions and through regular monitoring by the Funding Council of institutions' financial returns. Any universities facing heightened challenges to their financial sustainability are subject to a higher level of engagement.

Impact assessments

Equality and diversity

5. There are no equality and diversity issues associated with this paper.

Island communities

6. The recommendations in this paper do not have an impact on island communities.

Carbon reduction

7. There are no carbon reduction issues associated with this paper.

Publication

8. This paper will be published on the Council website in edited format (to remove references to specific institutions or forecast information) as it includes information which, if disclosed, would be prejudicial to the effective conduct of affairs (Freedom of Information (Scotland) Act 2002, Section 30).

Further information

9. Contact: Andrew Millar, Assistant Director, Institutional Sustainability and Governance, tel: 0131 313 6538, email: amillar@sfc.ac.uk.

University Sector Private Placement Borrowing

Purpose

10. The purpose of this paper is to **consider** institutions' arrangements for the repayment and monitoring of their Private Placement borrowing.

Background

11. In recent years, universities have significantly increased the use of Private Placements as a method of financing. With banks (traditionally the biggest lenders in the university sector) halting new loans because of capital requirements that were introduced in the aftermath of the 2008 financial crisis, and the European Investment Bank halting new loans because of Brexit, private funding deals have accounted for the vast majority of additional borrowing in the university sector in recent years. The format of this type of borrowing involves large bullet repayments of capital at set points over the term of the borrowing with interest being paid in the intervening years.

12. The university sector reported total borrowing of £1.718bn at the end of July 2021. Of the total sector debt as at 31 July 2021, £945m (55%) related to Private Placements. The current level of Private Placements for the seven institutions[1] which use this method of financing, is set out in **Annex A**. The table highlights that the bullet repayments are due to be made over the period from 2027 through to 2057.

Questionnaire

13. We recently asked the seven institutions to:

- provide high-level information to build our understanding of their position on Private Placements; and
- receive assurance on their arrangements for addressing the consequent future capital repayments.

{1x paragraph}

Key findings

14. The key findings from our analysis of institutions' questionnaires and recent correspondence are as follows:

[1] Heriot-Watt University, Robert Gordon University, University of Aberdeen, University of Edinburgh, University of Glasgow, University of St Andrews, University of Stirling

- Private Placement lenders are mainly large pension funds and are no less rigorous, with covenants and covenant reporting on a par with traditional debt. Detailed due diligence is carried out by the lenders with annual reports and covenant calculations checked annually by external auditors which give assurance over institutions' ability to repay interest. Long-term bonds are seen as the only type of borrowing with more onerous requirements.
- Institutions are in regular contact with Private Placement lenders, generally every six months, to keep lenders informed on their financial status and plans. This is more relationship maintenance rather than something that is sought by lenders.
- Institutions have no immediate plans to renegotiate Private Placement financing though that may be a route that some will follow with all options being evaluated closer to the time that the bullet repayments are scheduled. For most institutions, this is some distance away.
- The focus in the short to medium-term for a small number of institutions may be on repayment of European Investment Bank debt which is regarded as a more expensive form of financing.
- Four institutions have either set up, or are in the process of establishing, a loan servicing fund for the purpose of managing Private Placement repayments. They have acknowledged that these funds may not be fully sufficient to cover all future bullet repayments and additional payments may be considered should financial capacity allow. The retention of long-term investments and other risk management tools may also provide effective mitigations over the long term. The establishment of a loan servicing fund has been a condition of borrowing consent provided by SFC to institutions in recent years.
- The absence of a loan servicing fund is not necessarily a sign of bad debt management. Institutions have reported that a loan servicing fund may not be the best use of capital and it may be preferable to invest cash in universities' activities to earn a better return.
- Most institutions have not set up formal monitoring mechanisms in relation to the loan servicing fund rather this is covered through management accounts, treasury management reports and other financial performance reports to institutions' governing bodies.
- Institutions do not anticipate having to renegotiate covenants with lenders.
- Most institutions currently have no plans to put in place further Private Placement finance.

Conclusion

15. There are no immediate concerns about institutions' ability to make future capital repayments against Private Placements and it is reassuring to note progress made in establishing and monitoring of loan servicing funds. {1x paragraph}

Next steps

{1x paragraph}

16. SFC will continue to request regular updates on loan servicing funds so that we can be assured that robust arrangements are in place for addressing future capital repayments. We have also arranged meetings with Bank of Scotland and Barclays in early December and will be meeting soon with the Office for Students Lenders Group to keep appraised of latest developments. Regular updates will continue to be reported to the Committee.

Recommendation

17. The Finance Committee is invited to:

- **Consider** the update based on an analysis of questionnaires recently returned by institutions.
- **Note** and comment on the proposed next steps.

ANNEX A

{1x paragraph / table}