No easy answers: English student finance in the spending review

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Introduction

Many people would like to see more public spending on education. The arguments for this rest partly on the financial benefits and partly on the non-financial benefits; they also rest partly on the benefits to society and partly on the benefits to individuals. The diagram below shows some of the proven benefits of higher education across these four dimensions. [1]

SOCIETY

Society / Non-market:

- Greater social cohesion, trust and tolerance
- Less crime
- Political stability
- Greater social mobility
- Greater social capital

Society / Market:

- Increased tax revenues
- Faster economic growth
- Greater innovation and labour market flexibility
- Increased productivity of co-workers
- Reduced burden on public finances from co-ordination between policy areas such as health and crime prevention

NON-MARKET — MARKET

Individual / Non-market:

- Greater propensity to vote
- Greater propensity to volunteer
- Greater propensity to trust and tolerate others
- Lower propensity to commit (non-violent) crime
- Better educational parenting
- Longer life expectancy
- Less likely to smoke
- Less likely to drink excessively
- Less likely to be obese
- More likely to engage in preventative care
- Better mental health
- Greater life satisfaction
- Better general health

Individual / Market:

- Higher earnings
- Less exposure to unemployment
- Increased employability and skills development
- Increased entrepreneurial activity and productivity

INDIVIDUAL

The education sector constantly strives to convey the benefits of spending more to policymakers. This will, and should, continue; indeed, there are strong arguments for doing even more to convey the benefits of education.[2] However, given the competing demands on the UK's public finances and competing political priorities, it is unwise for the higher education sector in particular to assume more public spending is inevitable or even probable.

Policymakers have promised more spending on research, some of which is likely to benefit universities (although the increases are not guaranteed and research is generally a loss-making activity).[3] Beyond this, they have suggested other parts of the English education system, such as further education colleges, are more deserving of extra resources than universities.

Indeed, there are indications that higher education institutions in England are more likely to be on the receiving end of cuts rather than the beneficiaries of spending increases. For example, Gavin Williamson, the Secretary of State for Education, has:

- opposed the old expansionary target of sending half of all young people to higher education;[4]
- condemned 'dead-end courses that leave young people with nothing but debt';[5] and
- not ruled out the Augar report's recommendation from 2019 to lower tuition fees.[6]

Saving money

When it comes to educating undergraduate students, there are three main ways to reduce public expenditure: cut the number of funded places; spend less on each student; or lower the proportion of student loans that are written off.[7]

More specifically, the available options include:

i. imposing new student number caps, either in general or indirectly by limits on specific courses or via the imposition of minimum entry standards;

ii. cutting teaching grants to institutions or lowering tuition fees / loans; and

iii. tweaking the parameters of student loans, such as raising interest rates (as recommended by some students' unions), lowering the repayment threshold (as recommended by at least one former Universities Minister) or lengthening the repayment period (as recommended in the Augar report).[8]

Of these three options, Jim Dickinson of Wonkhe has written:

> *If we think of this as some kind of Bermuda triangle with student numbers, the unit of resource and the contribution scheme all in play, it's clear that the latter will have to contribute its fair share to whatever goal is being set by the Treasury. I'd add that the more that the first two are shown to be difficult in practice, the more chance we end up with the contribution scheme carrying more of the weight.*[9]

A decade ago, there was a fourth option too: shifting payments made to institutions for teaching students from arriving predominantly in the form of grants to arriving as extra student fees (backed by loans). At the time, student loans did not count as public spending even though some of the loans were expected never to be repaid. So as a result of reducing the teaching grant to universities and increasing tuition fees and loans to fill the gap, as occurred in England in 2012, in-year spending on higher education fell dramatically. The abolition of maintenance grants in England in favour of higher maintenance loans in 2016 also had an impact in the same direction.

Subsequently, the loan system was made more generous when the student loan repayment threshold was increased from £21,000 to £25,000 in 2018, lowering the expected repayments.

Since then, student loans have been reclassified, meaning every pound lent out that is expected never to be repaid, amounting to over half of the total, counts as current public spending.[10]

The accounting change not only reversed much of the previous savings but also gave policymakers a new incentive to look for savings. This has come to look even more urgent as graduate salaries have come under pressure, meaning repayments could amount to less than modelled.

Some people believe the increase in the write-off costs, which is known as the Resource Accounting and Budgeting (RAB) charge, pulls the rug from under the whole system of student finance in England. For example, a HEPI paper by Alan Roff concludes:

> *While one can respect the skills of the Office for National Statistics in producing a solution to restore reporting accuracy to the national accounts, it is not sustainable to retain a loan and debt repayment system in which loans are not loans, debts are not debts and repayments are not repayments.*[11]

Others take a more evolutionary approach. Edward Peck, the Vice-Chancellor of Nottingham Trent University and a member of the 'independent panel' known as the Augar review, recently summed the current situation up like this:

> *One of the central challenges that all of those with a stake in higher education face is the rising cost of the [student] loan book. The government has been silent on Augar's recommendations on student contributions, in particular lowering the threshold for starting repayments. This would go a long way to reversing the deepening financial hole.*[12]

The *Guardian* has similarly argued that some tweaks could bring the system back into equilibrium:

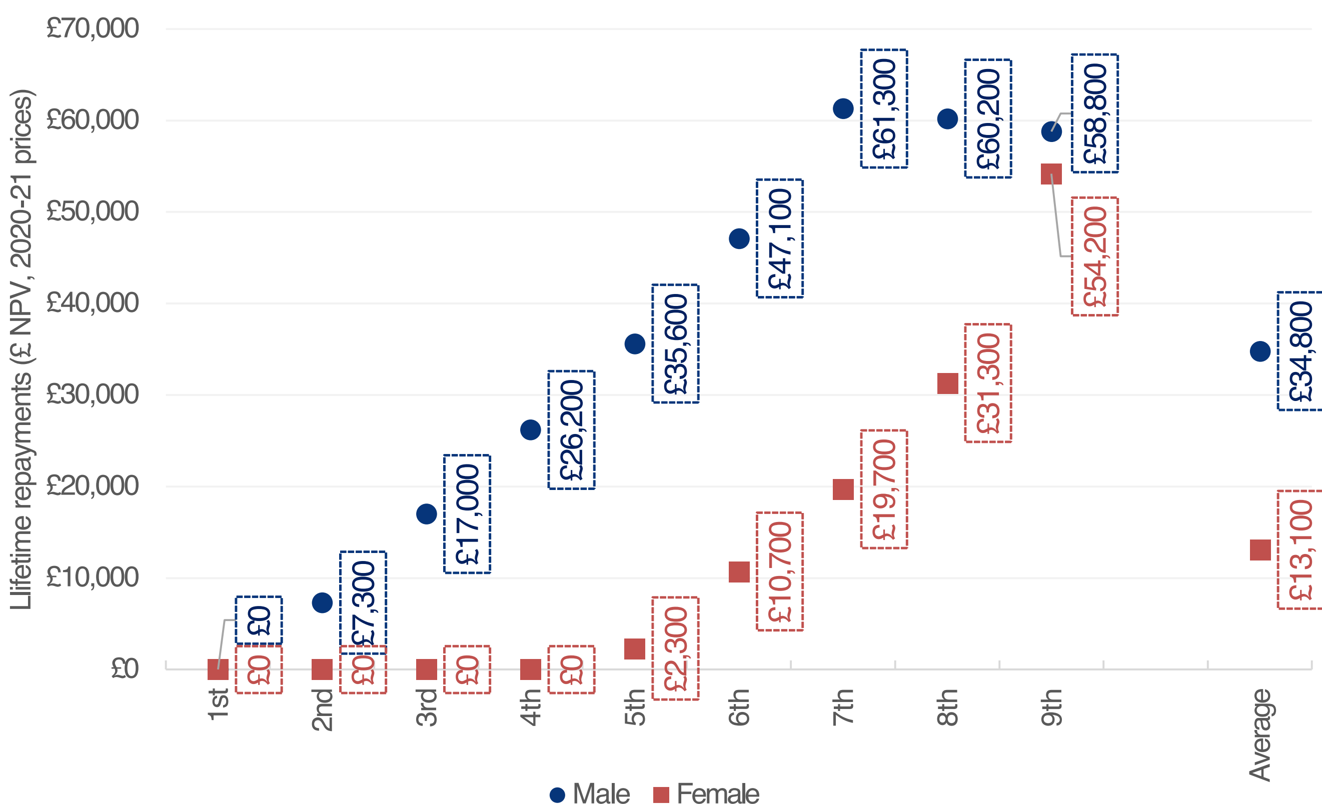
> *Among the options discussed is a cut to the annual tuition fee, from £9,250 to £7,500, as suggested by the Augar review of tertiary funding two years ago. Other measures would increase the amount that graduates repay, by extending the repayment window from 30 years and lowering the income threshold for repayments.*[13]

Some options

HEPI commissioned London Economics to model some alternative parameters for student loans in England, including removing real interest rates, an increase to the repayment period and reducing the repayment threshold. The first of these options would increase the cost to Government while the other two would reduce it.

The modelling focused on the undergraduate cohort of English-domiciled students commencing their studies in 2020/21 on either a full-time or part-time basis (as well as EU-domiciled students attending English higher education providers). The cost for this cohort over their entire expected period of study approaches £11 billion, split between £5.4 billion on tuition fee loan write-offs, £4.0 billion on maintenance loan write-offs and £1.2 billion on the residual teaching grant (paid by the Office for Students to institutions). The average debt on graduation is expected to be £47,000 and the proportion of loans written-off (the so-called RAB charge) is likely to be 54%, as around 88% of former students are expected not to repay their full loan while one-third (33%) are expected not to repay any of their debt.

Total loan repayments by full-time undergraduate degree graduates by earnings decile and gender (net present value) in 2020/21 prices



Repayments vary substantially by gender – due to the graduate gender pay gap[14] – with male former students repaying just under £35,000 on average while female former students repay just over £13,000. This indicates that an increase in repayments will often affect women proportionately more.

Removing the real rate of interest: Interest is applied at its maximum rate of 3% above the Retail Price Index on student loans during the period of study. Afterwards, the real rate of interest is tapered, so in 2020/21 people on incomes below the repayment threshold faced no interest above inflation and those on £47,835 or more faced the maximum amount of interest. Abolishing the real rate of interest, which is thought by some policymakers to be a particularly unpopular feature and which has been described by Chris Skidmore MP as 'out of all proportion to the reality of current interest rates', would have an annual cost of £1.2 billion.[15] The impact would be regressive, helping only the best-paid graduates. As the Money Saving Expert, Martin Lewis, has pointed out, under the current rules, 'you only pay any interest if you earn enough to have cleared the amount you originally borrowed within the 30 years. If not, you're just repaying the amount borrowed, not the interest.'[16] It would also benefit men, whose repayments would fall by an average of £6,400, more than women, whose repayments would fall by £1,300.

Extending the repayment period from 30 years to 35 years: Unlike removing the real rate of interest, an extension to the repayment period would save the Government money. Extending the repayment period would have no impact on graduates with the lowest incomes, who would continue to repay nothing, nor on graduates with the highest incomes, who would continue to repay their entire loan balance before even the original 30 years had elapsed. However, it would affect those in between. The Augar report recommended a 10-year increase: 'we believe borrowers should continue to repay their loan for as long as they benefit; we judge this to be 40 years after study has ended.'[17] However, we have modelled the more modest change of an increase to 35 years. This offers a saving of just under £1 billion and reduces the RAB charge by around four percentage points to 50%.

Reducing the repayment threshold to match the repayment threshold for pre-2012 student loans (from £26,575 to £19,390): It has been claimed that the decision to increase the repayment threshold to its current level offered poor value for money. The Augar report, for example, said: 'We question the justification for a system which excludes so much of a borrower's earnings from any repayment and which helps to reinforce the "no win, no pay" element in student choice.'[18] People who studied on the old loan system, before £9,000 fees and loans were introduced, faced a lower repayment threshold in 2020/21 of £19,390. If this repayment threshold were to be extended to those who currently face the higher threshold, then it would reduce the cost of one cohort of students by almost £3.8 billion, split by £2.2 billion less on tuition fee loan write offs and £1.6 billion less on maintenance loan write offs. This would have the impact of reducing the loan write off (the RAB charge) from 54% to 33%, which is roughly the expected rate when the current system was introduced. It would also reduce the proportion of former students who do not repay their entire loan from close to nine-in-ten (88%) people to three-quarters (76%), as well as reduce the proportion who never repay a penny by more than half from 33% to 16%. Both male and female graduates would repay an average of around £10,000 more.

The impact of these different options are shown below and further information on them, plus some additional options, are outlined in more detail in a slide pack produced for HEPI by London Economics, which is available at www.hepi.ac.uk and www.londoneconomics.co.uk.

	Current system	No interest above inflation	35-year repayment term	Threshold of £19,390
Cost of fee loans	£5.4 billion	£6.1 billion	£4.9 billion	£3.2 billion
Cost of maintenance loans	£4.0 billion	£4.5 billion	£3.7 billion	£2.4 billion
RAB charge	54%	61%	50%	33%
Percentage not repaying all	88%	74%	85%	76%
Percentage not repaying any	33%	33%	33%	16%
Average debt	£47,000	£45,600	£47,000	£47,000
Average repayments male	£34,800	£28,400	£37,900	£44,700
Average repayments female	£13,100	£11,800	£15,500	£23,500

Conclusion

Many people believe that more should be spent on higher education, especially at moments of profound upheaval like the current one, when the labour market is changing fast, when the number of school leavers is growing and when the per-student unit of resource has been eroded by inflation over the past decade.[19]

But this is not how many people outside of the education system see it and, if they cannot be persuaded to avoid cuts to higher education spending, then it is important that lots of modelling occurs to see the different possible outcomes.

Different options have profoundly different outcomes but it is possible to discern some general rules of thumb. In particular, cuts to student places will make it harder for universities to deliver the transformation in widening participation expected of them by the Government and others, and less income for universities is likely to have a broad impact on the role that universities play in society.[20] While the headline tuition fee tends to be the focus of considerable debate, with many calls for it to be reduced, students are more concerned about the day-to-day cost of living.[21]

Tweaks to student loans designed to raise repayments from graduates do not affect everyone equally. Many changes that have been proposed affect those on middle to high incomes most, as the lowest paid graduates do not have the means to repay and the highest paid graduates already extinguish their entire debt. Different tweaks have differential impacts on men and women, depending on what the change is.

Back in 2010, when the current system was put in place, policymaking happened very fast as a result of the timing of the independent Browne review and the political and fiscal cycles, with all the key decisions being taken between the publication of the Browne report in mid-October 2010 and the votes in the House of Commons in early December of the same year.[22] While the system put in place back then has proved more resilient than many people predicted, this year there is more time to consider the details. We should use it well.

Endnotes

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