Item 5

Shareholder Committee
Market Update – Education Sector
4 September 2018

1.0 Purpose of Report

1.1 The purpose of this report is to provide an update to the Shareholder Committee on the market position of the education sector. It covers information on the trading environment with particular emphasis on increased competitor activity and reducing school budgets. The report also details what impact this has on the Brierley Group and what risks and opportunities exist.

1.2 The academies agenda, along with maintained schools becoming more autonomous has led to schools becoming more discerning in the services they purchase. This report will specifically cover two aspects of the education sector, namely increasing financial pressure in the system and also the agenda around conversion to academy status.

2.0 Pressure on School Budgets

2.1 The changing school environment has occurred during a period of increased pressure on school budgets. Funding to schools in recent years has been static whilst staffing rates of pay has increased.

2.2 Examining the financial impact of the annual one per cent pay settlement for school staff, for all state-funded mainstream schools (including local authority maintained, academies, free schools, etc.) a report by Kreeston Reeves (February 2018) found nationally that:

i) Funding allocated by the government through its new National Funding Formula for schools (NFF), fails to meet pressures on schools budgets produced by this cost alone. This is despite the announcement of an extra £1.3 billion in funding for schools by the government in July 2017.

ii) As many as 40 per cent (around 7,500 schools) are unlikely to receive enough additional government funding in 2018-19 to meet these pay pressures alone. For 2019-20, this proportion rises to nearly half of state-funded mainstream schools in England (around 9,000 schools).

iii) Schools are facing a variety of cost pressures, yet this analysis shows how many schools are struggling just from this staffing cost alone. In addition, our assumption of one per cent staff pay increase over the next two years is cautious – with the government having signalled that future rises in teachers' pay may be higher than the current one per cent cap over the next few years.

2.3 Closer to home, in this financial year, the new national funding formula has been implemented which on the whole should benefit schools in North Yorkshire. However, the level of gains for North Yorkshire schools are relatively small and are generally in line with inflation. However there are also a number of schools who are losers in the new formula and for these schools the level of losses are much greater than the increases benefiting the schools which are gaining in the new formula. This is particularly impacting on smaller secondary schools.

2.4 As well as changes in the funding formula, our rural schools are seeing reducing pupil numbers. As pupil numbers are the key drive for funding this will have a detrimental impact on their income. Analysis by North Yorkshire County Council suggests that should current funding arrangements and budget limitations continue maintained schools in North Yorkshire are increasingly likely to be in a deficit position. Without changes to schools the current projection forecasts that in 3 years 60% of schools in North Yorkshire are expected to be in a deficit position.

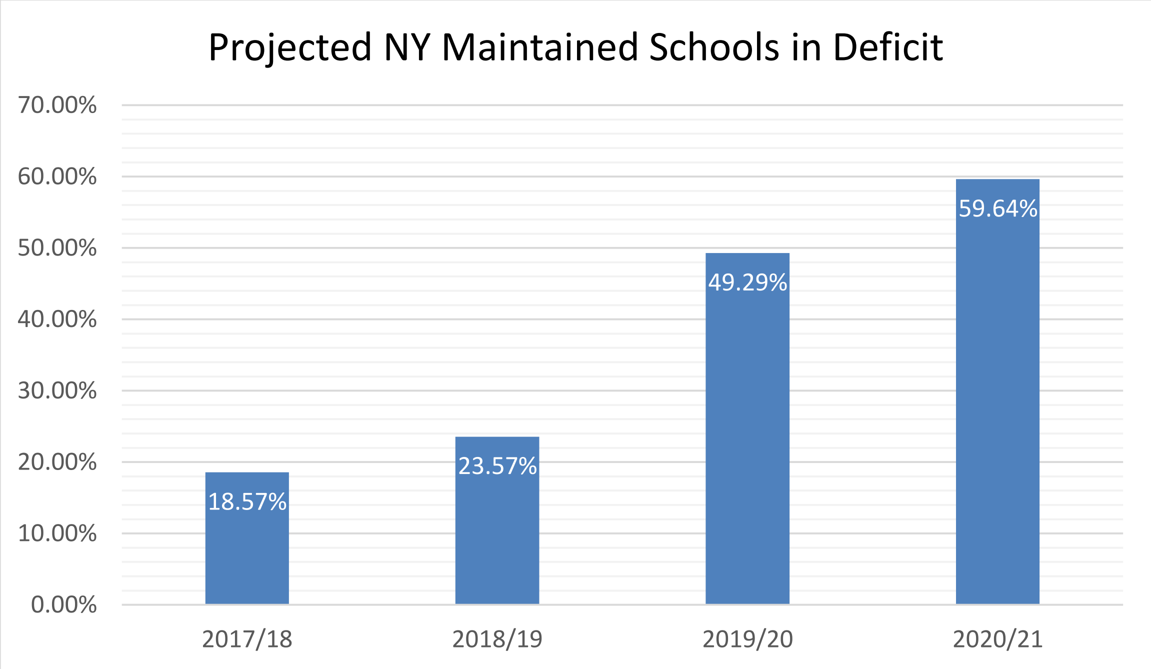


Chart 1, source: NYCC Financial Management Service

2.5 This projected deficit position in North Yorkshire reflects a trend which has occurred across England in recent years. In the period of four years up until 2016-17, the proportion of local authority secondary schools in deficit nearly trebled, expanding to over a quarter of all such schools.

2.6 The number of local authority maintained primary schools in deficit has also risen. In 2010-11, 5.2 per cent of local authority primary schools were in deficit; in 2016-17, the proportion of primary schools in deficit increased significantly, to 7.1 per cent. The average primary school deficit also noticeably increased, from £72,042 in 2010-11, to £107,962 in 2016-17.

2.7 A conclusion to draw here is that not only are the number of schools in deficit increasing but also the extent to which they are in deficit is rising. Whilst the above information is only for maintain schools, it is a similar picture across the whole sector.

2.8 Schools are already taking steps to address these issues, as it is not a sustainable position in the long term – something has to give. Analysis conducted by the Education Policy Institute (EPI) in March 2018 shows that approximately two thirds of local authority maintained secondary school spend is directly on education, as shown in chart 2. Assuming there will be no additional funding available, a conclusion can be drawn that schools will be required to reduce spend in two areas: direct education and/or support services.

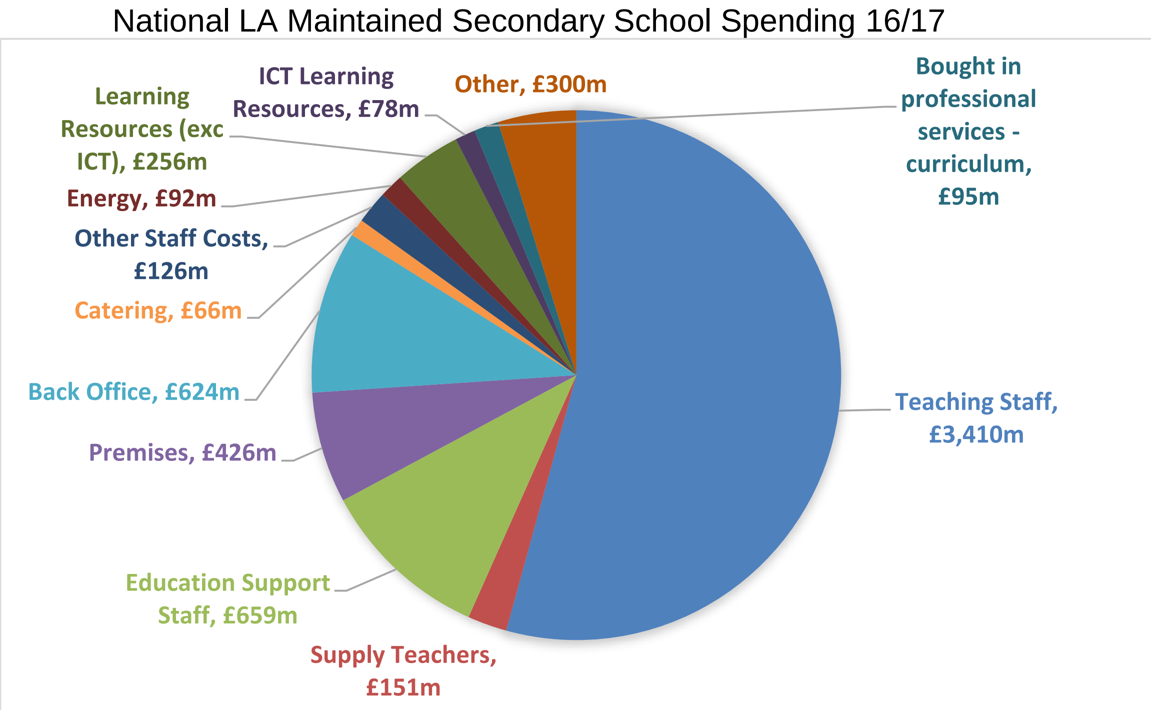


Chart 2, source: EPI March 2018

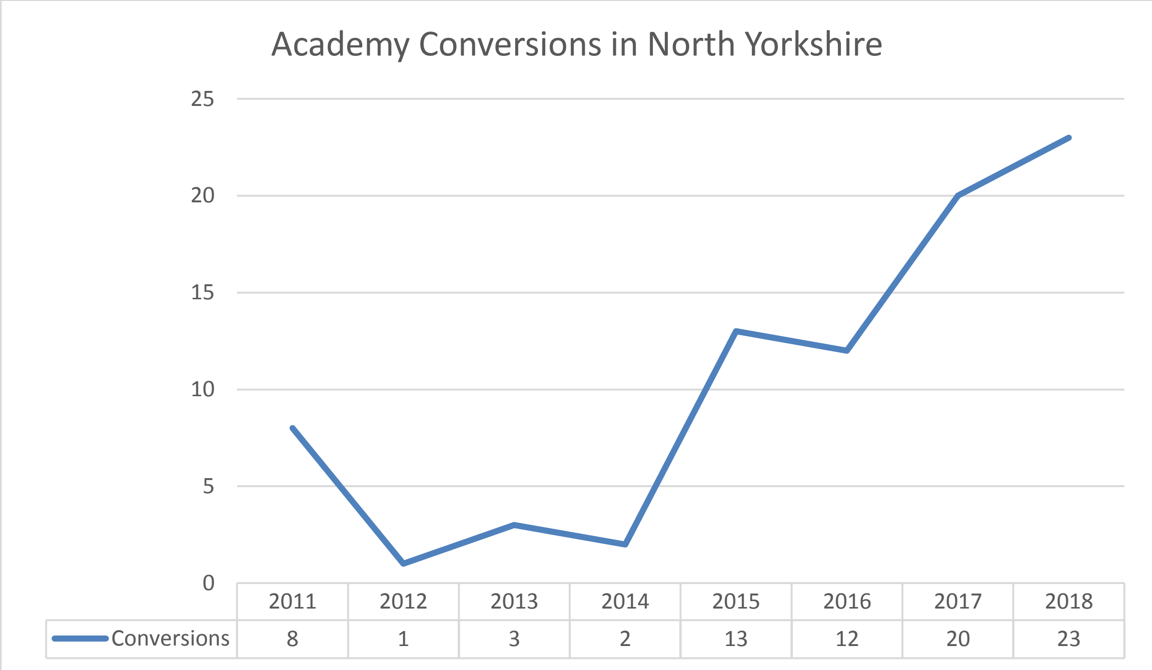
3.0 Academy Status in North Yorkshire

3.1 The following data obtained from the Department for Education shows a breakdown of maintained schools, single academies and multi trust academies in comparison with the City of York and National data. North Yorkshire currently has a larger percentage of maintained primary and secondary schools in comparison with York and All of England and considerable lower percentage of single academies.

	Maintained Schools			Single Academies			Multi-Academy Trusts		
	NYCC	York	All Eng.	NYCC	York	All Eng.	NYCC	York	All Eng.
% of Primary Schools	79%	56%	47%	8%	42%	22%	13%	2%	30%
% of Secondary Schools	56%	0%	47%	7%	34%	22%	37%	66%	31%

Table 1, source: DfE 2018

3.2 The following graph shows the number of conversions within North Yorkshire since 2011. The trend has seen an increase since 2015; whilst it is difficult to predict an exact forecast of conversion rates, a reasonable conclusion is that we can expect more conversion in the coming years, with six primary and two secondary schools indicating conversion in the next six months.



3.3 Statics obtained from the Education Policy Institute show less expenditure on professional services for converted academies than maintained schools, however this is 2015-16 data, and it is expected that 2016-17 data may show a reduction in the amount MATs are spending on professional services as they become more established:

2015-16 All England Expenditure for Bought In Professional Services (% of total budget)	
Primary Maintained Schools	2.10%
Primary Single Academies	0.80%
Primary Multi Academies	1.20%
Secondary Maintained Schools	1.50%
Secondary Single Academies	0.61%
Secondary Multi Academies	0.80%

A recent report issued by the Education Policy Institute titled

"School Funding Pressures in England states that "another approach to increasing efficiency which the government may continue to promote is for more schools to joint MATs. In some circumstances, joining or establishing a MAT may enable schools to find economies of scale".

We therefore need to understand the impact upon future sales targets and use data intelligence to predict which services are likely to lesson in demand as more conversions take place. It is important to note that there may be both opportunities and threats, depending on the nature and maturity of MATs. There are two types of MAT:

- Established Trusts – these are a threat to Brierley Group companies as they are an established group of schools which manage the services of the schools entering into them via a head office. They often have in-house staff to deliver the services we offer which means when a school joins they give notice to a lot of our packages, particularly the higher value ones.

- New Chains – these do not usually have arrangements already in place and are therefore more likely to be interested in Brierley services and retain business initially but leave as they grow.

- Whilst larger chains of MAT's have generally been seen as a threat to Brierley Group services, they can also represent a potential opportunity. Contracts for larger chains of MAT's are typically procured via a tendering process. Through the revised commercial governance procedure, we are now better equipped at responding to and making the most of these bidding opportunities.

4.0 Competitor Activity

4.1 Academy Conversion
As shown in section 3.3, when schools convert to academy status, on average, the level of bought in professional services reduces. Typically, this involves schools bringing services 'in-house' as part of a MAT, given perceived economies of scale. If this trend continues then this is one of the main competitor risks to the Brierley Group.

4.1 As a result MAT's can be seen as a form of threat to Brierley Group's customer base. Academy chains in North Yorkshire have, to varying degrees taken some level of service 'in-house'. This has affected a range of our services including; Financial Management Services; Facilities Management, Property & Design Services; HR; Payroll; ICT and School Improvement Services. Services which are less affected by this are Legal and Internal Audit given there more bespoke nature.

4.2 As an example in North Yorkshire, the following trusts significantly reduced their take up of NYES services:-

- Red Kite Academy Trust (7 schools in North Yorkshire)
- The Enquire Learning Trust (4 schools in North Yorkshire)
- Ebor Academy Trust (7 schools in North Yorkshire)
- Outward Academy Trust (3 Schools in North Yorkshire)

4.2.1 To a lesser degree, The Dales Academy Trust (10) and The Hope Learning Trust (3) also reduced their service take up.

4.3 Whilst the above is a risk area, it is also important to understand that the size and form of MATs are not common. For example, the majority of academies in North Yorkshire are part of a smaller MATs. Retention levels at these smaller MATs has been relatively high. We have also had sales success with smaller MATs outside of North Yorkshire.

4.4 Direct Competitors
In addition to this, and generally resulting from 'commercialisation' of the sector, there has been an increase in the number of private and third sector organisations promoting services to schools. This has particular prevalence in high volume, low margin services such as cleaning and catering. However, it is not limited to those services, with general market uptake in typically higher margin products and services, such as HR & Legal.

4.5 Competitor analysis across all products and services offered by the Brierley Group shows that the sector is crowded with no clear market leader locally or even nationally. Naturally this means it is a competitive environment and challenging to gain a share of 'market voice'. However, there is an opportunity if there is rationalisation of providers across the sector.

4.6 Comparing quality and cost between Brierley Group and competitors is not clear cut, there is a perception that the private sector has more flexibility when it comes to pay and pension. However, a good indicator of value for money is that the level of private sector involvement within North Yorkshire is still comparatively low when compared with bordering authorities, with the majority of schools in North Yorkshire retaining services offered by Brierley Group.

4.7 There are some specific examples of competitor activity in the region:

i) One local company has assisted converting 119 schools across the North of England since 2011. They continue to work with a number of converted schools, particularly across the Tess Valley area to provide professional services.

ii) In addition, other private sector companies have been commissioned to provide services by the bordering local authorities for the maintained schools in their area. Examples of this would be in Middlesbrough and York where two large, private sector organisations have taken on services on behalf of the authority. However, it is worth noting that these particular contracts are no longer in place.

iii) More broadly following the collapse and liquidation of Carillion in January this year, there is a growing perception surrounding private sector outsourcing. Whilst Carillion, and other large providers, typically target larger clients than single schools; it should be noted that confidence in the industry as a whole has been impacted. It is difficult to estimate to what extend exactly at this stage, however there is anecdotal evidence that customers are tendering for smaller and shorter contracts as a result.

5.0 Impact on Brierley Group

5.1 As Brierley Group is predominantly providing support services to the education sector, it should be anticipated that its customers will be under significant pressure to achieve increased value for money across all spend areas. This represents risks but also opportunities across the traded entities with the Group.

5.2 Risks:

i) There is a clear risk that as a schools comes under increased financial pressure, they reduce all spending which will have a direct impact on the amount they buy in. This extends to all suppliers including Brierley Group services. An important point to understand here is not just the number of schools in deficit but the extent to which they are in deficit (as described in Section 2). Analysis from 2016/17 showed that on average schools in deficit in North Yorkshire had an average negative revenue balance of £78.7k. Nationally, the comparison figure for that year was £131.2k. So whilst the position is relatively healthier in North Yorkshire, the pressure still remains. Additionally, at a national level in 2016/17 maintained primary schools in total spent 112% of their net budgets, whilst equivalent maintained secondary schools spent 116% of their net budget.

ii) As noted in section 4, as schools convert to academy status the overall trend is that more services are brought in-house. Exactly how this might impact on Brierley Group over the coming years in not clear, as the speed of both schools converting and when they choose to bring service in-house is not pre-determined. In other words, whilst the general trend is increasing number of Brierley Group customers converting to academy status, decision of bringing in-house will be determined by individual schools.

5.3 Opportunities:

i) Whilst schools are under financial pressure, it can be viewed that a simplistic response is to only reduce spending, however to date schools have various approaches when dealing with cost pressures. Some example include increasing teachers' contract time, class sizes and the amount of teaching undertaken by senior staff, amongst others. The opportunity is for Brierley Group to provide value-add support to schools, notably financial advice, which can assist in addressing cost pressures without simply cutting budgets.

ii) As the trend indicates the number of schools in North Yorkshire converting to academy status is rising, as such there is an opportunity to provide support to aid them through that process.

iii) When consider the impact of Carillion, Brierley Group has an advantage when compared generally to the private sector. The motivation and drivers behind the entities within the Group, given its ownership structure, set it aside from some of its competitors.

iv) Like schools, local authorities are also under increasing financial pressure, as a result a number have reduced or even retracted services offered to schools in their areas. This creates an opportunity for Brierley Group, working with North Yorkshire County council, to develop relationships with those authorities and help support schools in that geography. Some examples include Hartlepool BC reducing it Health & Safety and Educational Visits Advisory Service; and City of York Council no longer providing cleaning and catering.

6.0 Recommendation

6.1 Members are asked to note the report.

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