Scoping report for union branches, University of Sussex

26 May 2020

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Overview

I have prepared this scoping report for the unions at University of Sussex by reviewing the publicly available documents, in particular the financial statement that forms part of the annual report.

I have not had sight of any more recent financial information and so, of necessity, some of the conclusions about the financial health of the institution rest on data that is nine months out of date.[1] I have seen materials prepared by the union branches at Sussex and reports in the local, national and industry papers, so have an understanding of what is being proposed by management in response to the threats to recruitment and retention presented by the current pandemic.

I am most concerned about the reported covenants on Sussex's borrowing, for, primarily, the £100m private placement bond taken out in 2017. According to the vice-chancellor this requires the university to run a *surplus every year*.[2] Further clarification provided by the Director of Finance to staff indicates that this clause is based on net operating cash flow, with a minimum of just over £12m required each year to cover interest payments (c. £7.5m) and repayments of principal (c. £2.3m) and an additional margin of 25 per cent.

This target provides more leeway than "surplus" (the excess of income over expenditure in the accounting period) as net operating cash flow benefits, for example, from the exclusion of depreciation. At Sussex depreciation is over £20m, which means that figures for "surplus" are typically at least £20m below net operating cash flow each year (once pension provision adjustments are excluded).

If it is indeed a level to be achieved *every year* (and not, for example, breached more than once in three consecutive years or exceeded in average over such a three-year period, which would be typical covenants reflecting that events happen), then it represents a restrictive imposition on the university's ability to navigate the crisis. It is very possible that the clause was agreed to for the

[1] English universities use a financial year that runs from August to July. The most recent financial statement was published in December and covers the year to 31 July 2019.

[2] http://www.sussex.ac.uk/staff/newsandevents/?id=52023

sake of marginally lower interest rates on the bond and savings of a few £100,000 pa. At any rate, it was an unwise decision. That Sussex have moved so quickly compared to other universities (and seem to be making a virtue of "acceleration") is probably a result of this covenant.

The university is currently quoting a "scenario" in which Sussex faces a £71m hit to income (£38m from a reduction in international students, £13m from a reduction in Home/EU students, and £20m from lost accommodation fees).[3] Apparently, this scenario is only meant to illustrate the potential shock coming in the Autumn and does not form the basis for current budget plans. It would represent the loss of over 50% of full-time international student tuition fees and over 10% of all fees from full-time Home and EU students.

It is important for the university to provide staff with what their current budget plans *are* and to evidence the savings envisaged from the Finance Review Guidelines.[4]

Sussex would not be able to manage an impact such as that in the quoted scenario, while also protecting its covenant status, *without serious damage to its ability to bounce back*. In order to avoid a breach of covenants in 2020/21 under whatever circumstances, the university might have to make damaging cuts where other institutions, without such restrictions on autonomy, could suffer losses but absorb the short-term difficulties using cash reserves. Sussex risks turning a short-term hit into a medium-term crisis. Whoever signed this clause gave away the ability of Sussex to manage the current crisis appropriately.

In a worst case scenario for international recruitment, the alternative — finding the necessary in-year savings for 2020/21 — may be beyond the university. In particular, it should be borne in mind that redundancy programmes do not generate significant *immediate* savings owing to consultation, notice periods and financial compensation. This exacerbates the dangers in trying to cut a way to "surplus" in 2020/21.

The university should be opening discussions with creditors regarding the covenants. It would not normally be in the interests of long-term lenders to demand damaging short-term cuts as it would jeopardise the university's sustainability. But this is an unusual scenario, and potential bondholders such as insurance companies may have pressing demands of their own, which would lead them into hard negotiating positions.

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[3] http://www.sussex.ac.uk/staff/newsandevents/index?id=51915

[4] The updated risk register (ARC-13-2 May 2020) scores recruitment as a 25, indicating that the impact on recruitment is both "highly likely" and "highly damaging", that is over £25million.

In the worst case, the university may face demands for accelerated repayment of the bond including interest. Sussex has not spent its bond proceeds and might even be able to meet the entirety of this potential liability today, given its holdings of current investments and cash. That said, university management should be talking to government about a potential bailout loan in case bondholders do wish to have all their money back, if the university is at the same time wrestling with large shortfalls in income in 2020/21. The university would not be able simultaneously to repay its borrowings and absorb a large hit to income.

Unions at Sussex should be demanding sight of the bond contract and the legal advice the university has received here regarding the status of the bond covenants in a pandemic. The university needs to recognise now the point at which it would need outside help. It is preferable to avoid breaching covenants, but not to the extent that compulsory redundancies lead to reduced capacity for future years, when numbers are expected to recover. The university should act *as if* it is facing a short-term challenge; if it proves not to be, then *it will be outside the scope of any but a handful of wealthy, elite universities to handle it on their own*.

Any income hit greater than £50m is probably the point at which it should consider preparing to breach its covenants and seeking government support. This is my estimate based on last year's financial statement and is only offered as a loose indicative figure in the absence of a proper forecast and budget.

I would stress that more information about the scenarios and envisaged savings is required and, in the interests of good industrial relations, Sussex unions should be requesting what is needed for negotiations in such a difficult time (scenarios that aren't being used as the basis for budgets are not helpful). Clauses in recognition agreements should cover such provision.

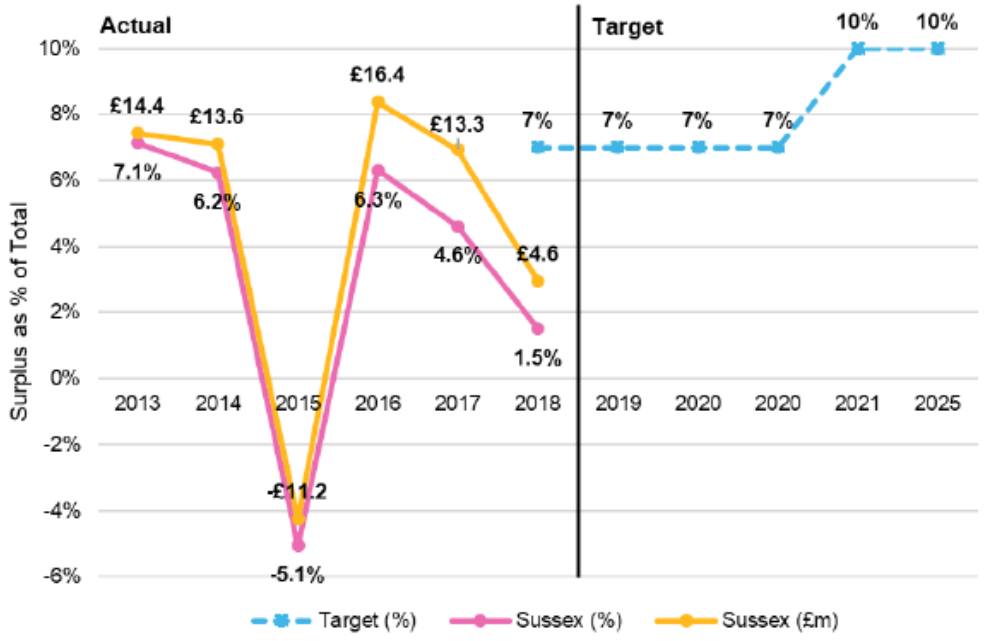
Financial Headlines

Sussex is a rapidly growing institution (it has doubled its turnover in the last decade). With an income of £324million in 2018/19, it is just outside the top 30 UK HEI's on that score.

In the last financial year, it recorded a loss of £22m, but, like all universities participating in the USS pension scheme, this was distorted by an adverse movement in the value of the provision that Sussex is required to record on its balance sheet. Without that £44*million* adjustment, Sussex would have recorded a comprehensive *surplus* of £22m.[5]

At 7.4% of income, this surplus figure is just above the only financial target included in Sussex's suite of Key Performance Indicators. This target of 7% has been in place since May 2018. Sussex last achieved this in 2012/13 (7.1%).

The chart shows Sussex's surplus as a % of total alongside the £000s values and targets.



November 2019, Council paper C-247-4, "Annual KPI Update for Council"

The surplus target was due to increase to 10% from next financial year. Overall, the English HE sector makes surpluses in the region of 2-3%, only a minority of larger universities manage to deliver surpluses above 5% consistently and many struggle to break even. These targets are therefore demanding both historically for Sussex and relatively across the sector.

[5] "The comprehensive loss of £22m is reported for the year as a result of a £44m pension adjustment due to provisions relating to the USS pension scheme. Good underlying performance however generated a £43m operating cash surplus towards the essential investment into the University's infrastructure identified within the strategy." 2018/19 Financial Statement, p. 5

University management have recognised that the planned increase in this target would place the institution under strain, even before the advent of coronavirus.

> "These targets have been set in order to provide the cash resources required to deliver the new strategy, including investment in the capital programme (across both our physical estate and our information technology provision), investment in new academic initiatives and as some protection against the significant risks the higher education sector is currently facing that are outlined further below. Delivering this level of surplus will be challenging."
> **2018/19 Financial Statement, p.10**

One of the themes of this scoping report will be the overly ambitious capital development programme, which, as in the paragraph above, appears to be the key driver for strategic decisions. Sussex's underlying finances are sound but the plans to bring together £300m of funds for capital development in the five years to 2025 would have placed the institution, teaching in particular, under strain, even before the advent of the pandemic.

Debt

Sussex is relatively indebted. Council has set a maximum limit to external borrowing of £200million for the group. The university owes £180m. The majority, £100m, comprises three private placement bonds issued in 2017. These run through to the 2040s; until then the debt is "non-amortising": the university only pays annual interest on the bonds, roughly £2.75m per year; the first repayment of principal, £50m, is due in 2044.

The other loans come to c. £80m and are split between Lloyds and Barclays. Again, the second loan (Barclays) appears to be interest-only, while the university is repaying about £2.3m per year to Lloyds on top of interest.

Included in loans are the following:

LENDER	AMOUNT OUTSTANDING AT 31 JULY 2019 £'000	TERM	INTEREST RATE %	BORROWER
Lloyds	40,647	to 2034	5.815	University
Barclays	40,000	to 2039	5.85	University
Private Placement Loan Series A	50,000	to 2044	2.76	University
Private Placement Loan Series B	18,000	to 2049	2.78	University
Private Placement Loan Series C	32,000	to 2049	2.84	University
	180,647			
Barclays	656	to 2022	6.21	Sussex Innovation Centre Development Co Ltd.
Total	181,303			

2018/19 Financial Statement, p. 46

Total annual interest payments come to c. £7.5m pa. In 2039 (Barclays), 2044 (bond) and 2049 (bond), Sussex will be repaying £40-50million. By 2025, this will begin to impinge on the planning horizon of the institution.

The issue here is not so much the level of debt, though at 55 per cent Sussex is above the sector mean and median of about 30%. The issue is the agreements into which Sussex entered in order to secure the borrowing and to improve the interest charged.

I always recommend identifying the covenants on borrowing as they limit the university's autonomy. Loan covenants may require the university to meet certain financial performance targets or give lenders rights to veto further borrowing or sales of significant property. A breach of covenant can lead to the imposition of worse terms, the "acceleration" of repayment, or in the worse case, there may be demands to repay borrowing *immediately*.

As mentioned in the introduction, an email from the vice-chancellor (15 May) has indicated that the university has signed up to a covenant with lenders that requires it to make a surplus each year.[6] When the vice-chancellor says that the university is legally prevented from using reserves to cover losses, this is inaccurate. What he means is that the covenant prevents the university from running losses *in the first place*. Or more accurately strongly dissuades the university from running a deficit.

Universities aim to make surpluses, so this might not have appeared overly burdensome when it was agreed, but it is restrictive and in unusual times exacerbates the situation, as it makes it harder for the university to absorb short-run losses in order to preserve capacity.

The existing debt may also prevent Sussex from accessing (or limit its ability to access) further coronavirus support measures later in the year. For example, if the government develops some kind of loan scheme specifically for universities along the lines of Coronavirus Large Business

[6] 'As I said last week, these are difficult times and the scale of the challenge should not be under-estimated. Although we have some money in the bank, *we are bound by legal agreements to make a financial surplus every year* (before technical adjustments) and this means that we can't use our reserves to cover losses. This is why, for example, we have suspended all but essential spending on the University's estate. However, at a meeting of Senate this week I reassured colleagues that compulsory redundancies would be a last resort for the University.'
http://www.sussex.ac.uk/staff/newsandevents/?id=52023

Interruption Loan Scheme (CLBILS).[7] Such schemes may require relatively rapid repayment and may be seen to impinge on the ability of the institution to repay its already existing borrowing.[8]

Could Sussex repay its borrowings?

At 31 July 2019, Sussex was still holding most of the bond proceeds (despite the bond having been taken out in 2017), which accounts for its unusually high liquidity (see further discussion below). It may seem outlandish to suggest that Sussex consider handing back the money tied to the problematic covenant, but the damage (to medium and long-term) that could be done by trying to run a surplus next year should not be underestimated. Moreover, pursuit of a surplus after a big drop in recruitment might put the institution on a collision course with unions in 2020/21 given the cuts that could be required. It would be very hard to advise students to study at Sussex at such a time.

Even if it is the case that Sussex would be committed to £2.75m bond payments for 25 years, that price might still be better than extensive cuts today. What must be weighed in the balance is the potential lost income resulting from lower capacity: this could be much greater than £2.75m per year.

Covenants

I understand that Sussex has two main covenants on its lending: one measures indebtedness, the other the ability to service debt.

The first involves the ratio of external borrowing to net assets (excluding the £80m pension provision): roughly £180m : £430m or 0.41:1.[9] Sussex is apparently required to maintain that ratio below 1:2 (0.5:1). On that score, Sussex's net asset position could deteriorate by c. £70m without breaching this covenant. This represents significant leeway.

The second covenant is more problematic. Sussex is required to meet an annual debt cover ratio of 1.25:1. This means that its net operating cash inflow must be sufficient to cover payments of

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[7] https://www.gov.uk/guidance/apply-for-the-coronavirus-large-business-interruption-loan-scheme
My understanding is that universities are eligible for this scheme at present, but the loans are offered at commercial rates of interest.

[8] "The chancellor's allies said the Treasury would not initially look to take equity stakes in struggling companies, some of which do not have investment-grade credit ratings and cannot access a Bank of England commercial loan scheme. *The preferred option would be to extend loans that ensured that the taxpayer was at the top of the hierarchy of creditors.*" (my emphasis)
"'Project Birch' plan to bail out stricken UK companies", *Financial Times*, 24 May 2020
https://www.ft.com/content/9d1dd8ff-c978-44c0-8e60-f50de8e8e641

[9] For the purposes of Sussex, net assets is equivalent to general reserves.

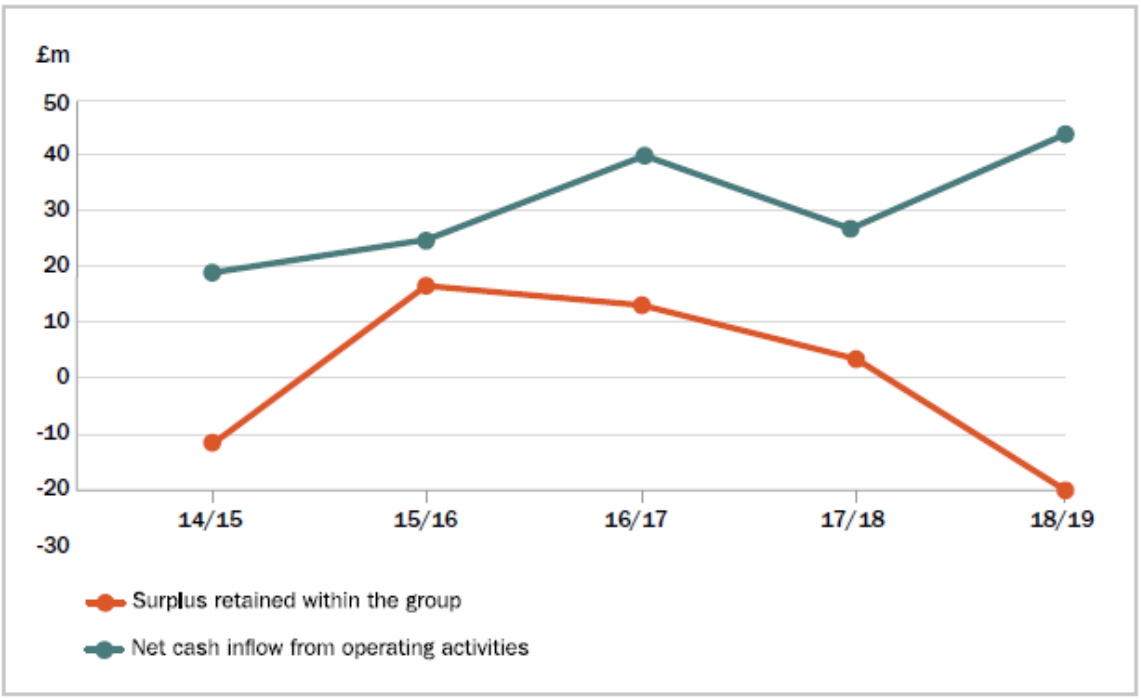
interest (c. £7.5m pa) and repayments of principal (c. £2.3m pa). Sussex therefore appears to need a net operating cash flow of at least £12.25m pa to meet this pledge.

Net cash inflow from operations excludes expenditure like items like depreciation and so should always be significantly higher than overall surplus or deficit (income minus expenditure), when pension provision movements are excluded from the latter.[10]

I provide detail here in order to illustrate a key point: Sussex management's stated intention is to pursue a surplus. If they achieve that, then they should hit the second covenant given the way that net operated cash inflow is derived. I would like to suggest that there is a bit more leeway here: that Sussex could run a *deficit* of around £10m and still meet its covenant.

Sussex's surplus (excluding pension adjustment) was about £22m in 2018/19, but its net operating cash inflow was £43m. The following chart, which includes pension movements in "surplus", published in the most recent annual statement shows this relationship. Net cash inflow in blue is significantly higher than surplus.

SURPLUS AND NET OPERATING CASH



2018/19 Financial Statement, p. 5

[10] A large beneficial pension movement could increase surplus above net cash inflow.

If Sussex is in fact required to use a form of "adjusted" net operating cash flow (ANOC), then there may be further leeway. In 2017, the Higher Education Funding Council for England in collaboration with the British Universities Finance Directors Group developed an ANOC measure, which was then used as the basis to assess increases in borrowing.[11] The particular definition of ANOC was:

	Net cash flow from operating activities
+	Cash received from investment income
+	Endowment cash received
-	Cash paid on interest on borrowings
-	Cash paid on interest element of finance leases
=	**Adjusted operating cash flow**

FSSG *Report on the Evaluation of the 2014-15 Annual Sustainability Assurance Report pilot*, September 2016, Annex A

I do *not* believe Sussex is using this exact definition in its debt cover ratio as that would lead to double-counting: what is paid out in interest would appear in both sides of the ratio. But if, for illustrative purposes, we plug the relevant values from Sussex's 2018/19 Financial Statement into this calculation then we see that there might be some additional margin for meeting the covenant.

	£000s	Running Total
Net Cash from Operating Activities		**43,451**
+ Cash from Investment income	2,386	45,837
+ Endowment Cash Received	867	46,704
- Cash paid on interest element of finance leases	351	46,353
= Adjusted operating cash flow		**46,353**

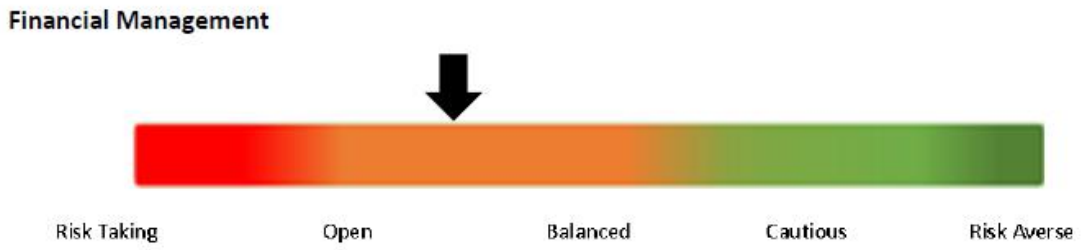
Calculations based on **2018/19 Consolidated Cash Flow Statement**, p. 28

[11] From August 2017, universities needed to gain Hefce's permission to increase borrowing beyond a multiple of ANOC. See *Financial Sustainability Strategy Group Newsletter*, July 2017

Unions at Sussex should demand sight of covenants and specific detail on the calculation used. Even if investment income and endowment cash are way down in 2020/21, there may still be significant sums involved that mitigate the need for some cuts.

That management have not yet provided a forecast scenario towards which they are planning, nor any appropriate figures by which to assess savings or these covenants is a red flag. Vague gestures in their direction seem only designed to intimidate rather than illuminate. It is very important to understand that Sussex has made its life more difficult than those of its peers by signing up to such tight covenants. It is not in control of its destiny and must hope for a drop in income of no more than half the size of the scenario management have been discussing publicly. That might be manageable, but Sussex must also take care not to avoid medium-term self-harm through misguided adherence to its covenants. Sussex has a difficult task but must make the choices it faces clearer: it may be better under certain conditions to breach covenants. It should be open with Office for Students and the Department for Education about the particular problems it has.

In its risk appetite statement, Sussex rates its approach to financial management as somewhere between "open" [to risk] and "balanced" on a five notch scale.



Risk Appetite Categories	Influence upon the University's objectives in order to protect against financial and reputational impacts and safeguard our legal position
Risk Averse	It will be undesirable to take risks as there is no benefit to be gained from risk taking. Strong controls will be introduced to treat any unavoidable risks that may arise.
Cautious	Limited exposure to risk will be closely monitored and controlled as risk taking may have undesirable consequences leading to a decline in performance/sustainability.
Balanced	Risk may be taken, following careful analysis and with appropriate treatment and ongoing monitoring.
Open	Risk will be taken in order to develop, improve performance and be competitive, with proportionate levels of control.
Risk Taking	Exposure to risk will support the fulfilment of key strategic priorities. Controls will support creativity and innovation as there will be significant benefits from risk taking.

Statement of Risk Tolerance & Risk Appetite(C-247-16), p. 5-6

This is unusual. Most universities present their financial management as "risk averse" or "cautious", even when they aren't. As charities, universities are expected to act prudently with finance.

> "Prudence, beyond what is expected in a commercial operation where business risk is of the essence. In a charity, *risk is a necessary adjunct to delivering public benefit* - a key distinction. Future investment decisions need to be soundly based and carefully assessed, with your HEI investing enough in people, property and systems to survive and prosper. The governing body should ensure that tomorrow is not sacrificed for today."
> Getting to Grips with *Finance,* Leadership Foundation for HE 2009

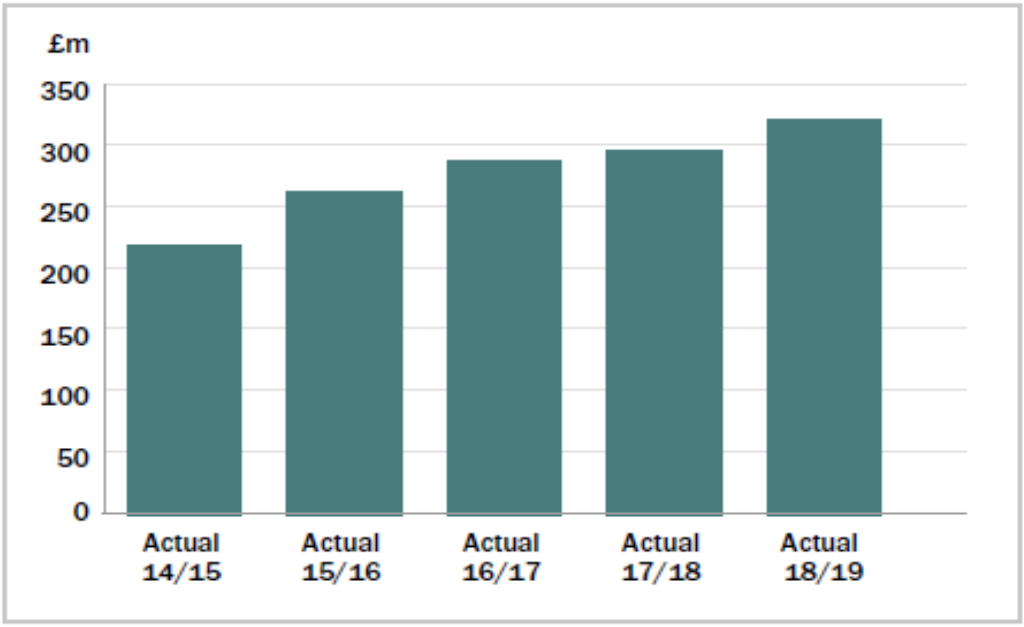
This should be borne in mind when considering references to "challenges", "strain" and "tension" in discussions with the University executive. These risks would have been exacerbated by plans to expand further. "Today" can also be sacrificed to a misplaced vision of the future. And we are now in a situation where risk should be minimised.

Growth

I would also note that the extremely striking growth exhibited by Sussex (in both the last decade and its plans through to 2025) suggests that the university is moving towards becoming a teaching-led institution, more similar historically to a former Polytechnic in size and proportion of income from tuition. This is likely to demand changes to academic staffing and contracts to be sustainable. Attracting a further 4000 students, even without the impact of the pandemic, would likely require a lowering of entry tariffs and significant reorganising around retention. It is very hard to see how these plans can be continued and talk of "acceleration" likely refers to contingency plans that were being developed in case the planned expansion did not occur. These are unlikely to achieve significant savings for 2020/21 and anything too committal should be best left until things are clearer and calmer.

The 2018/19 financial statement includes the following chart showing the last five years of annual turnover. Even within that relatively short period, Sussex has increased its income by over £100m.

TURNOVER



2018/19 Financial Statement, p. 6

I have included an extract from the 2011/12 Financial Statement that shows that the institution brought in less than half current levels in 2008/09.

	2011/12	2010/11	2009/10	2008/09
	£m	£m	£m	£m
Income	**182.7**	174.9	165.9	158.6
Expenditure	**169.0**	163.6	165.7	160.3
(Deficit)/surplus for the year before disposal of assets	**13.7**	11.3	0.2	(1.7)
(Deficit)/surplus for the year after disposal of assets	**13.7**	11.3	0.2	(1.6)

2011/12 Financial Statement, p, 2

At the time, in a talk to Sussex UCU in February 2013, I noted that Sussex management appeared to have grasped that it was much better to be bigger in the new funding and market regime.

This was probably the right call, but this growth does not now appear to be sustainable. The most recent financial statement indicates the strain on the estate,[12] while Sussex's expenditure on staffing (pension provision adjustments excluded) has dropped below 50% of total, with concomitant rise in the percentage of fixed term contracts in use.

From 2017/18 to 2018/19, tuition fee income rose by 10% and student FTE by 7.4%, 'driven by a intake of 8,697 new students, which was 9% higher than the previous year' (2018/19 Financial Statement, p. 7).

Current Senate papers discuss increasing the student body by another 4,000, taking FTE numbers to over 22,000.[13] It seems clear that this growth in student numbers is required to generate internal funds for capital development.[14] Sussex therefore appears to be locked into a cycle:

1. capital development is needed to redevelop a campus that is no longer suitable for the current number of students (after strong growth);
2. but that capital development can only be funded by growing student numbers even further;
3. repeat.

It is harder to find an academic rationale for this and there would be a danger of "lock in" were it not for the disruption resulting from the pandemic.

That said, it does appear as if numbers were likely to stagnate, if not decline, in September 2020. Sussex's numbers in *2019/20* (as at end of October) were only 2% up on the previous year at 18,270, compared to 17,927 FTE.[15] In particular, targets for OS PGT students were missed by

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[12] "The significant growth in students and staff over the past five years now means that the continued expansion of our operations is constrained by the space available to accommodate new initiatives. In order to address this, a number of major capital projects are in progress or are being planned. We are developing Estates and IT roadmaps to set out our intended priorities through to 2025." 2018/19 Financial Statement, p. 10.

[13] 'S-259-5 Turning the Dial Paper', March 2020.

[14] "We are ambitious in our vision but, as always, Council is also conscious of its duty to protect our financial sustainability for the benefit of future generations. … For this reason, Council spent time considering a potential growth in student numbers, and how this would align with the vision of Sussex 2025. We agreed that the University should develop its thinking on how student numbers might grow by several thousand up to 2024/25. In this way, Council believes the University can maintain its financial sustainability whilst meeting the strong need to ensure our infrastructure, services and environment are optimal for the students and staff of today and tomorrow."
http://www.sussex.ac.uk/broadcast/read/50472

[15] Council Paper C-247-6 Student Number Forecast 2019_20

over 250 FTE. The increase in Foundation students to 160 for both Home / EU and OS, also points to a changing focus for the university.

At the Professoriate meeting of 20 April management reported a drop in Home and EU undergraduate applications of over 20%, along with declines in overseas and postgraduate and "damagingly low" conversion rates in some parts of the Sciences and some areas of Arts and Humanities. Complaints about more prestigious universities taking numbers off Sussex add to concerns about what might happen in August, given that the government's imposed recruitment cap will be unlikely to protect universities of Sussex's standing (op. cit §§3.1-3.5). These caps include EU students with Home, and it is the opinion of many analysts that EU students are more likely to behave like OS students come the Autumn.

I understand that these caps will be based on forecasts of student numbers submitted to the Office for Students in December, rather than historic numbers plus 5%, though we have yet to have official confirmation of the exact allocations. Unions should request from management the numbers they submitted.

Cash Reserves

There is an unfortunate ambiguity in accounting terminology. "Reserves" or "general reserves" should not be confused with *cash* reserves, which only form a part of the former. For universities that are not for-profit (and therefore have no equity), reserves can best be understood as the excess of assets over liabilities: that is, equivalent to "net assets". That is, the university owns, or is owed (assets), more than it owes (liabilities). The vast majority of the value in a university's assets will be land and buildings. These will often be valued at historic cost or deemed cost and subject to depreciation. They might well not raise those values recorded in the accounts, if they were sold (and indeed there might be very little market for some of these assets).

When judging a university's ability to absorb shocks, it is better to concentrate on *unrestricted* funds that are held as cash, "near cash" or as investment assets that could be readily sold such as equities (i.e. "liquid" assets). Some funds are restricted in that they are the result of endowments that require them to fund certain specific activities, bursaries or posts. Some investments represent funds sunk into joint ventures or subsidiaries: as such they cannot be readily converted into cash.

At 31 July 2019, Sussex held c. £118m in current investments, of which £13.6m was restricted. These investments are mostly in the form of deposits.[16]

NOTE 7 CURRENT INVESTMENTS

	YEAR ENDED 31 JULY 2019 CONSOLIDATED £'000	YEAR ENDED 31 JULY 2019 UNIVERSITY £'000	YEAR ENDED 31 JULY 2018 CONSOLIDATED £'000	YEAR ENDED 31 JULY 2018 UNIVERSITY £'000
Short term investment in shares	12,805	12,805	11,181	11,181
Short term deposits	105,022	105,022	164,217	164,217
	117,827	117,827	175,398	175,398

2018/19 Financial Statement, p. 45

On top of these, it holds cash and near cash of just over £100m.[17]

CURRENT ASSETS					
Stock		54	51	54	51
Trade and other receivables	6	30,596	42,880	29,298	41,390
Investments	7	117,827	117,827	175,398	175,398
Cash and cash equivalents		109,088	102,872	28,581	23,400
		257,565	263,630	233,331	240,239

2018/19 Financial Statement, p. 27

Excluding the restricted investments *and cash held by other group entities*, leaves around £207m.

This means that the university is very "liquid". The Charity Commission recommends that organisations should hold sufficient reserves to cover 90 days of expenditure for operational needs and to deal with temporary shocks. Removing depreciation and the pension adjustment, Sussex's 2018/19 expenditure was £280m. This means that Sussex has sufficient liquidity to cover roughly 260 days. 90 days would be roughly £70m, but Sussex itself seems to specify no minimum liquidity level.

This makes Sussex one of the most liquid institutions in the country. Were cash and near cash levels still at this level today, then Sussex would have a substantial cushion against shocks, *even if it were forced to repay its £100m bond.*

However, some of this cash will have been spent in the intervening months. It is imperative to identify current cash and near cash holdings. In the table above, the university had converted

[16] It holds very little non-current investments (£6.7m) and these are mostly sums invested in subsidiaries.

[17] "Cash includes cash in hand, deposits repayable on demand and overdrafts. Deposits are repayable on demand if they are in practice available within three months without penalty. Cash equivalents are short term, highly liquid investments that are readily convertible to known amounts of cash with insignificant risk of change in value. They include term deposits, government securities and loan stock held as part of the treasury management activities. They exclude any such assets held as endowment asset investments."
2018/19 Financial Statement, p. 34

almost £60million of investment holdings into cash and cash equivalents; the latter had increased by nearly £80m since July 2018. This suggests that cash was being raised prior to being spent on capital projects.

The accounts only indicate that Sussex had £13m of capital commitments (£5.3m contracted, £7.7m approved but not contracted).[18] But the change in composition of current assets suggest imminent spending on a larger scale.

It is important that capital investment also be suspended as far as possible. It appears that work will proceed on the Student Centre, which is due to open by Spring 2021 (Professoriate meeting, 20 April, §5.3). This appears to be costed at £15m of work remaining.

Recent comments from senior management suggest that less than £10m of what was available has actually been spent. This helps greatly. Sussex should prepare itself for a possible breach of its covenants in the next 24months, even if it does not plan to do so. Suspending capital works is sensible.

Capital Development Plans

Sussex management had hoped to use the £100m bond proceeds, plus accumulated internal funds to finance the majority of a £200-300m capital development plan by 2024/25 (this overall plan was approved by Council in March). This was extremely ambitious before the pandemic as it would have entailed running significant surpluses over the next few years (that 10% target described above).

These plans have been driving recent strategy. Here is one summary.

> The main source of funding for future investment has to come from surplus generated by the University. Director of Finance Allan Spencer says: **"**That's why our Council has agreed we need to achieve an annual surplus of around 7%, which is a surplus of circa £20 to £30 million."
>
> "Together with our current cash balances, these surpluses may provide up to £300 million for us to invest between now and 2025, in both estates and IT infrastructure."
>
> "While this may seem like we have a lot to invest, we know already from our detailed investigations that there is around £800 million worth of possible options identified - so as a community we have some tough decisions to make."
> http://www.sussex.ac.uk/strategy2025/estate-and-it-strategies

The plan to grow students to over 22,000 is largely driven by a desire to have £300m, rather than £200m to invest, rather than any academic vision for the university. At least as far as public

[18] 2018/19 Financial Statement, p. 49.

presentation of the strategy goes. It is very common for universities to lose sight of fundamental objects in the desire to pursue capital projects.

In addition, attention should be paid to the third party PFI-style deals that are being prepared for student accommodation, such as East Slope. These projects may represent a *further* £200-300m of development. Capital here is provided by third parties so that Sussex can avoid using its balance sheet capacity. In return, the university has signed or will have signed contracts with differing future financial liabilities.

East Slope is being constructed by Balfour Beatty and is funded through a separate *public* bond, which does not appear on Sussex's balance sheet.[19] In this case, Sussex appears to have agreed to guarantee rents for the early days of the project and that this amounts to over £9m for 2019/20 and 2020/21.

> "The University entered into contracts with Balfour Beatty Investments Limited ('BBI') in March 2017 in connection with development of student residences on the University's Falmer campus. … . The arrangement gives the University nomination rights on the student bedspaces, on an annual basis, a year in advance. Student rents will be set by reference to parameters set by the agreements. First delivery of bedspaces completed in Autumn 2018. The arrangements are treated as a Service Concession under accounting conventions and results in an annual liability and asset at each balance sheet date for any rooms nominated (and thus guaranteed for rent payment). *During the initial four-year construction period the University is required to nominate at least 75% of the available rooms each December for the following academic year. This commits the University to pay for these rooms.* It is anticipated that student rents received will fully fund this obligation. The University is entitled to participate in certain increases in rent income in ESRSA LLP and accounts for this gainshare on an accrual basis."
> [my emphasis]
> 2018/19 Financial Statement, p. 9

> "The total liabilities relating to the service concession included in the Balance Sheet as at 31 July 2019 were £9.3m (2018 £11.3m), representing the present value of lease obligations for the following two academic years."
> 2018/19 Financial Statement, p. 42

The accounting treatment which matches an asset and liability of equal value, *assumes that the accommodation places are taken up*. If they are not, then it appears that Sussex would still have to pay the £4.5m for the year.

[19] https://www.businesswire.com/news/home/20170402005044/en/Assured-Guaranty-Wraps-UK-University-Bond-Issuance

Corona Pandemic

While you might expect the pandemic to interrupt these plans and cause a reflection on the sustainability of the strategy and the institution, Sussex appears instead to be pursuing "acceleration".

An email from 25 March references a "comprehensive review" of expenditure:

> "This work was undertaken because we knew that we could not deliver on the much-needed investment in the student experience and in our research infrastructure, if we did not make big changes. … we need *to accelerate our timescales* on savings and to implement a suite of new and immediate measures on expenditure." (my emphasis)

Again, I believe that this position has been determined by the borrowing covenants and capital development plans, not by a circumspect or considered view of the institution's (likely) position. Sustainability is determined by the ability to withstand turbulence and manage shocks. Acceleration runs counter to the prudence emphasised above, particularly when the impacts are not yet known.

As outlined in a variety of press coverage, the university expects to break even this year (2019/20), at least £15m or so down on what it had planned. In 2020/21, it expects larger effects:

> "University of Sussex vice-chancellor Adam Tickell said the institute could lose £13 million if just one tenth of its British students defer their studies until after the coronavirus pandemic.
>
> "And he warned another £38 million could be lost if half its international students stay away. Hundreds of them have demanded tuition fee cuts in response to the crisis."
> *Argus*, 12 May
> https://www.theargus.co.uk/news/18440986.coronavirus-planned-sussex-university-job-cuts-panned/

These figures are consistent with the scenario quoted in the Overview, which had, in addition, £20m accommodation costs. Sussex is reliant on its £190m tuition fees for 60% of its income. Of that, international students contributed £70m in 2018/19, around 22% of all income. The figures cited in the above scenario represent significant reductions across new and returning students: over 50% of *all* Full-time Overseas Tuition Fee income and over 10% of *all* Full-time Home and EU fee income. Most scenarios I have seen elsewhere differentiate between deferral rates for new and returning students.

Sussex management have though denied that they are using this cited scenario as a forecast on which to base 2020/21 budgets.

You can see that the such hits to income would be too large for the university to handle. If we use the illustrative ANOC figure for 2018/19 of c. £45million, then a hit to income of more than £30m would threaten the covenant based on debt service cover ratio without cuts. A hit of £70m would make a covenant breach impossible to avoid without compulsory redundancies. The scale of such redundancies would be exacerbated given the costs associated with such a response. Although it would be preferable to avoid a breach of covenant, there is a point at which the measures needed to achieve that in 2020/21 would be so damaging to the university that the ability to return to normal would be threatened.

Universities should be looking to preserve capacity in the short-run. If this turns out *not* to be a short-run hit, then most of the sector will need bailing out. But individual institutions should in the first place treating it is a shock and identifying the level of shock that can be absorbed without the need to inflict further harm through cuts with longer term repercussions.

This all presents a particular problem for Sussex as its pre-covid plan was to grow further. It is hard to see how those plans can be "accelerated" given the scale of cuts that might have to be implemented to break even in 2020/21 (or indeed to hit its ANOC target of c. £12m). Universities that wish to "rebound" in future years need to protect as much capacity as possible.

It is hard to see how much would be saved in 2020/21 by cancelling agency contracts, associate lecturer and GTA contracts and allowing fixed-term contracts to expire. It is important to get figures from management on these estimates, as it will enable the unions to assess how much further saving might be needed under different scenarios *and what the consequences of such savings would be for future years*. These assessments should include the possibility of covenant breaches and potential demand for accelerated payment.

When faced with unknowns such as recruitment in September, it is reasonable to try to reduce costs. Other institutions are exploring offering staff unpaid sabbaticals and temporary reductions in working hours. But this has to be balanced against both loss of capacity (and therefore future income losses) and workloads that existing staff might have to endure if causal and fixed-term contracts are not renewed.[20] It is therefore important to see workload models that present how permanent staff will be expected to pick up the slack.

[20] Note though that this is a projected income cut owing to a fall in students, so some work will not be there as the number of students would have declined. This may seem an obvious point to make, but the problem facing the institution is not a "funding cut"; a decline in numbers is the potential problem. It's because there will be fewer students to teach that there will be less money available.

Sussex management should really provide a proper budget with an estimate of savings that will be generated by these proposed measures and agree an interpretation of "essential" that makes reference to workload, rather than, for example, "operational continuity".[21]

It is only with the provision of this additional information that options can be properly negotiated with staff.

[21] In Financial Review Guidance, the key term is "essential": 'if it is not contractual, mandatory or essential to the operational continuity of the institution, we would ask that you avoid incurring any costs.' Here it is qualified by "operational continuity", which is markedly different to, for example, "manageable workloads".