

# THE IMPACT OF REMOVING THE LONDON WEIGHTING

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Report prepared for London Higher

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## EXECUTIVE SUMMARY

The London Weighting<sup>1</sup> (LW) is an uplift paid to London higher education institutions (HEIs) to reflect the higher costs of providing services in London. London HEIs have received the LW for many years. The rationale for the LW is to recognise that providing a similar service in London is more costly than in the rest of the country, and that costs, such as staff salaries and property costs, are determined by local market forces that are mostly outside the influence of HEIs.

Similar uplifts to funding recognising cost pressures in London are applicable in other major public services, such as local government, education and health; in health, for example, a significant market forces factor adjustment is applied to the payments hospital trusts receive and this reflects the unavoidable higher costs of labour, land and buildings in London.<sup>2</sup>

Recent guidance from the Department for Education (DfE) to the Office for Students (OfS) suggests that the LW should be removed from the Strategic Priorities Grant (SPG) with immediate effect. The motivation for this recommendation is that the LW element of the SPG is seen as being inconsistent with the desire to level up the economy across the regions:<sup>3</sup>

*“The levelling-up agenda is key to this government, and we think it is inconsistent with this to invest additional money in London providers...”*

**Removing the LW is not an effective way to address inequalities across the economy.**

### 1. Some London boroughs are among the most deprived areas of the country

There is a huge amount of variation in the economic and socio-demographic composition of different parts of London. Income and wealth inequality in London runs high and **London boroughs are home to some of the most deprived areas of the country**. As Figure 1 shows, London boroughs are highly represented in the most deprived areas of the country, with a third of areas<sup>4</sup> being in the 30% most deprived parts of England.

London is home to a very diverse set of HE providers. There are 39 HEIs<sup>5</sup>, ranging from global institutions ranking in the top 20 in the world through to lower-ranking, teaching-focussed institutions which primarily educate local students.

The student intake at London’s HEIs is reflective of the diversity of the capital. Some institutions have strong international reputations and attract significant

<sup>1</sup> We use the term ‘London Weighting’ (LW) throughout the report to denote the sum of two elements of funding: (1) targeted allocations for students attending courses in London; and (2) the LW element of the student premium to support successful student outcomes.

<sup>2</sup> [https://improvement.nhs.uk/documents/475/Guide\\_to\\_the\\_market\\_forces\\_factor.pdf](https://improvement.nhs.uk/documents/475/Guide_to_the_market_forces_factor.pdf)

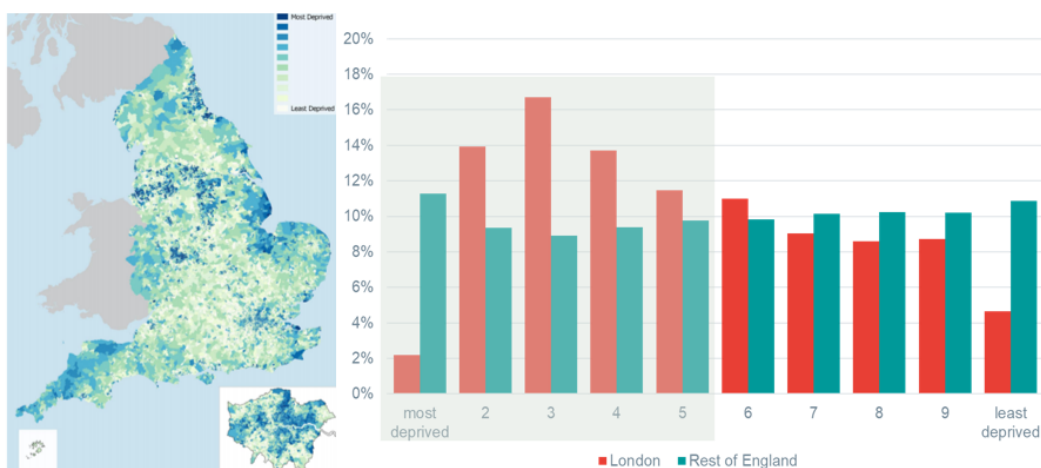
<sup>3</sup> <https://www.officeforstudents.org.uk/media/a3814453-4c28-404a-bf76-490183867d9a/rt-hon-gavin-williamson-cbe-mp-t-grant-ofs-chair-smb.pdf>

<sup>4</sup> Defined as Lower-layer Super Output Areas

<sup>5</sup> The analysis in this report focuses on institutions which mostly provide higher education (e.g. universities and higher education colleges). We use the terms ‘universities’ and HEIs interchangeably. Both refer to a list of HEIs identified as those for which the ‘Highest level of degree awarding powers held’ are Research and Teaching in the OfS register. When defining the list of London HEIs we have excluded HEIs primarily located elsewhere in the country which have a small London presence.

numbers of overseas students while others rely predominantly on home students. Recent research has highlighted that students from the lowest socio-economic groups are more likely to stay at their homes, rather than move closer to their place of study<sup>6</sup>. Many disadvantaged students who are often also commuter students attend their local London HEI. Removing the LW risks penalising such students since less funding is likely to mean less spending per student. It is important not to overlook the serious levels of deprivation in London, the diversity of HEIs in the capital and the role they play in the widening participation agenda.

**Figure 1 Index of Multiple Deprivation (IMD)**



Source: Frontier Economics analysis of Index of Multiple Deprivation (IMD), 2019 published by the Ministry of Housing, Communities & Local Government (MHCLG)<sup>7</sup>

Note: Proportion of Lower-layer Super Output Areas in different IMD deciles

## 2. Unit costs in London are significantly higher compared to the rest of the country

London universities have to spend more on staff, buildings and other costs. Staff costs represent around 55% of HEI expenditure on average.<sup>8</sup> In London, universities are contractually obliged to pay a London allowance to their academic staff, typically in excess of £3,000 per member of academic staff (full-time equivalent (FTE)). The London allowance applied to full-time *academic* staff alone therefore is likely to add at least<sup>9</sup> £80m to staff costs for London universities. More generally, the latest Annual Survey of Hours and Earnings (ASHE) data shows that median wages in London are between 20% and 30% higher than the rest of the UK.

The differences in costs are even more pronounced when it comes to other inputs such as land and buildings – analysis conducted by the Centre for Cities shows that the median rateable value per square metre in the capital is more than twice as high as the median value for England and Wales.<sup>10</sup> These input prices are set

<sup>6</sup> Donnelly, M. and Gramsu, S. (2018) Home and Away: Social, Ethnic and Spatial Inequalities in Student Mobility, London: Sutton Trust. Available at: [https://www.suttontrust.com/wp-content/uploads/2019/12/Home\\_and\\_away\\_FINAL.pdf](https://www.suttontrust.com/wp-content/uploads/2019/12/Home_and_away_FINAL.pdf)

<sup>7</sup> <https://www.gov.uk/government/statistics/english-indices-of-deprivation-2019>

<sup>8</sup> Calculated as the average share of staff costs over total operating costs over the period from 2015/16 to 2018/19 for all UK HEIs.

<sup>9</sup> In reality this number is likely to be higher since many non-academic jobs also receive a London allowance.

<sup>10</sup> <https://www.centreforcities.org/reader/city-space-race-balancing-need-homes-offices-cities/geography-demand-residential-commercial-space/>

in local regional markets; they are unavoidable and London HEIs are price takers in this regard.

The cost differences between London and the rest of the country have been well documented in previous research acknowledged in the OfS consultation on recurrent funding for 2021-22<sup>11</sup>. For example, research by Deloitte<sup>12</sup> for the Higher Education Funding Council for England (HEFCE) found that average academic staff costs in London were around 12-14% higher than the national average with the difference even more pronounced for non-academic staff costs. Recent KPMG<sup>13</sup> work has also found that provision in London is more costly relating to both academic and non-academic staff costs and also to land, building and maintenance costs.

The removal of the LW will therefore create an **uneven playing field** (in terms of unit costs) by requiring London's HEIs to absorb the consequences of being located in a conurbation with higher unavoidable unit costs.

### 3. The London HEIs that will be hardest hit can least afford it

The removal of the LW element of the SPG would result in a funding shortfall across London HEIs of around £64m or a 13.7% reduction in mean SPG<sup>14</sup> although the net reduction in funding (accounting for the redistribution of other grants) is likely to be just under £50m according to the OfS<sup>15</sup>. Removing this funding will create additional financial pressure for London HEIs and impact on their viability at a time when the sector is emerging from a global pandemic and other major policy changes such as Brexit – both are associated with significant risks for student recruitment, particularly international students.

All universities receiving LW funding will be affected by this proposal as the amounts of funding received are not trivial. However, given the significant variation in financial performance across institutions, it is likely that a number will be hit particularly hard. A number of London's HEIs already have deficits or are close to being in deficit, and removing the LW will push them further into the red (see Figure 2).

Many of these institutions are reliant on home undergraduate students and are less able to benefit from other revenue sources such as increases in international student numbers. Hence, the institutions which will be hardest hit are those that can least afford it.

*“We rely on tuition fee income and we have no other significant sources of funding which we could use to plug the gap. We would like to attract more international students but this requires investment and time.”*, Senior Leader of a London HEI

<sup>11</sup> <https://www.officeforstudents.org.uk/media/8610a7a4-0ae3-47d3-9129-f234e086c43c/consultation-on-funding-for-ay2021-22-finalforweb.pdf>

<sup>12</sup> <https://webarchive.nationalarchives.gov.uk/20180405115447/http://www.hefce.ac.uk/pubs/rereports/year/2017/regional/>

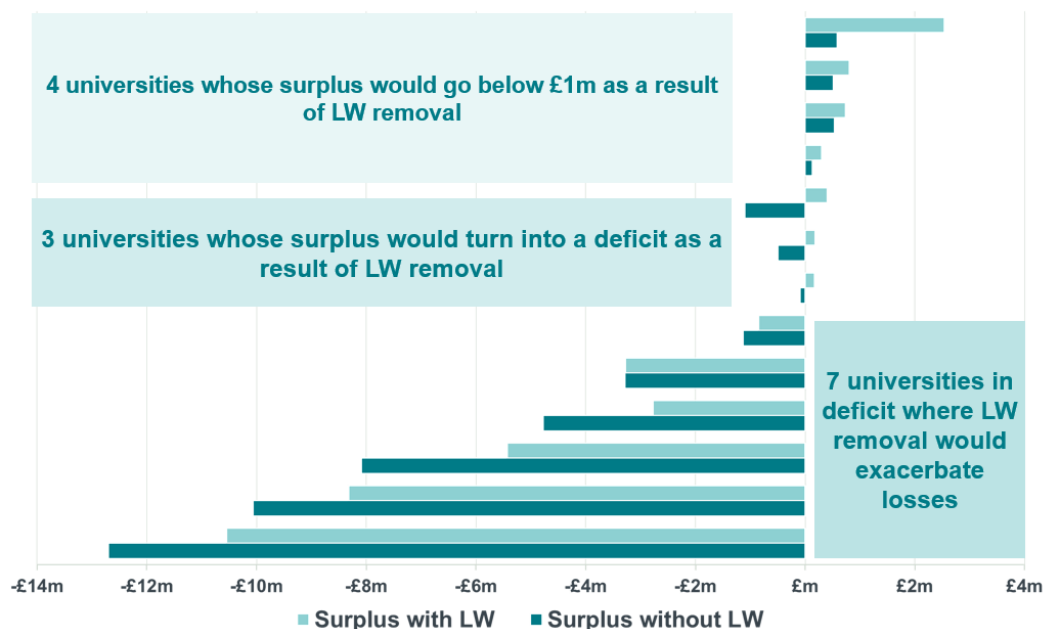
<sup>13</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/909349/Understanding\\_costs\\_of\\_undergraduate\\_provision\\_in\\_higher\\_education.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/909349/Understanding_costs_of_undergraduate_provision_in_higher_education.pdf)

<sup>14</sup> <https://www.officeforstudents.org.uk/media/a3814453-4c28-404a-bf76-490183867d9a/rt-hon-gavin-williamson-cbe-mp-t-grant-ofs-chair-smb.pdf>

<sup>15</sup> <https://www.officeforstudents.org.uk/media/8610a7a4-0ae3-47d3-9129-f234e086c43c/consultation-on-funding-for-ay2021-22-finalforweb.pdf>, Paragraph 46.

“This will most penalise those London universities which can least afford it. And it's taking away capacity that is primarily being accessed by under-privileged students.”, Senior Leader of a London HEI

**Figure 2 HEIs most heavily impacted by LW removal**



Source: Higher Education Statistics Agency (HESA) data FY2018/19.

Note: Figures for FY2018/19 are adjusted to account for the 2017 Universities Superannuation Scheme (USS) revaluation, as this expense is not a typical annual operating expense. Chart shows universities most affected by the LW withdrawal<sup>16</sup> but one with particularly high losses has been excluded to improve readability.

#### 4. HEIs with a teaching focus which train key workers and play an important role in widening participation in higher education (HE) will be particularly affected

HEIs which focus predominantly on teaching are likely to be disproportionately affected – these often train **key workers such as teachers, social care workers and medical staff**. Institutions offering such courses have a high ‘home’ undergraduate student intake. In London, these home students are also often ‘commuter students’ and disadvantaged students, so, bring with them added support needs. With tuition fee levels having been frozen in recent years, it is difficult for London institutions to recoup the costs of delivery. Some courses are loss making (undersubscribed and with low student numbers) but are provided because they feed into **shortage occupations for the NHS** – removing funding will make these types of courses even less viable.

“Some of our healthcare courses are of strategic importance for the NHS as they train workers in essential professions where there are workforce shortages. These courses can be loss making and difficult to recruit for.”, Senior Leader of a London HEI

Therefore, one unintended consequence of the LW removal could be a possible aggravation of the supply shortage of key workers in London’s labour market.

<sup>16</sup> We estimate that the remaining 24 London universities will have surpluses cut back by 8.5% on average.

The HEIs most vulnerable to funding cuts train large numbers of local students from difficult and disadvantaged backgrounds who require significant support to complete their education. Removing funding from these students may harm other policy objectives, such as **widening participation**, as these students are unlikely to move or travel elsewhere in the country to undertake HE.

*“The large majority of our students are from London; and the great majority are commuter students. These are students who cannot afford other universities. They’re commuting because they have no choice. They can’t afford to live on campus.”*, Senior Leader of a London HEI

## 5. Removing funding at short notice will have an impact on students

Removing significant funding at such short notice will leave those London HEIs most vulnerable to funding cuts with few options for absorbing the shock. Many have no cushion to fall back on so will have to cut costs, which in practice means cutting staff cost as other costs are harder to control in the short term. Reducing staff costs will mean reducing pay, where possible, or reducing headcount or some combination of both. Both have an impact on staff morale and the quality of service provided to students, ultimately **negatively affecting the student experience**.

*“Less money simply means less spend per student. We will have less to spend on the student experience as we’d be forced to reduce spend on things like staffing levels, capital projects, facilities and so on. In the end these things affect the student experience.”*, Senior Leader of a London HEI

*“Our financial resilience would be undermined. Our only option would be to cut staff costs and remove student enrichment opportunities and enhancement projects.”*, Senior Leader of a London HEI

## 6. Levelling down London is not the way to equalise economic performance across the regions

There is a strategic policy initiative to level up the regions in the UK and the education sector will play an important role in this. However, for all the reasons described above, taking funds away from London’s HEIs risks undermining the notion of a level playing field that the LW seeks to provide and, instead, will put London’s HEIs at a significant funding disadvantage compared to other HEIs elsewhere in the country. Some London HEIs, particularly those with a teaching focus and a relatively small international student intake will be disproportionately affected.

Taking away funds from London HEIs and spreading them across the country, potentially to areas and providers which are already relatively well off, is unlikely to help achieve the levelling-up policy goal. Particularly when many London institutions are already in deficit and domestic demand for HE in the capital is set to rise by 2035, with many ‘first generation’ students who are unlikely to move elsewhere pursuing a higher education.<sup>17</sup>

London is a major destination for international students accounting for around 30% of the England total. This clearly benefits local institutions and the economy. However, international students are not evenly distributed among London HEIs –

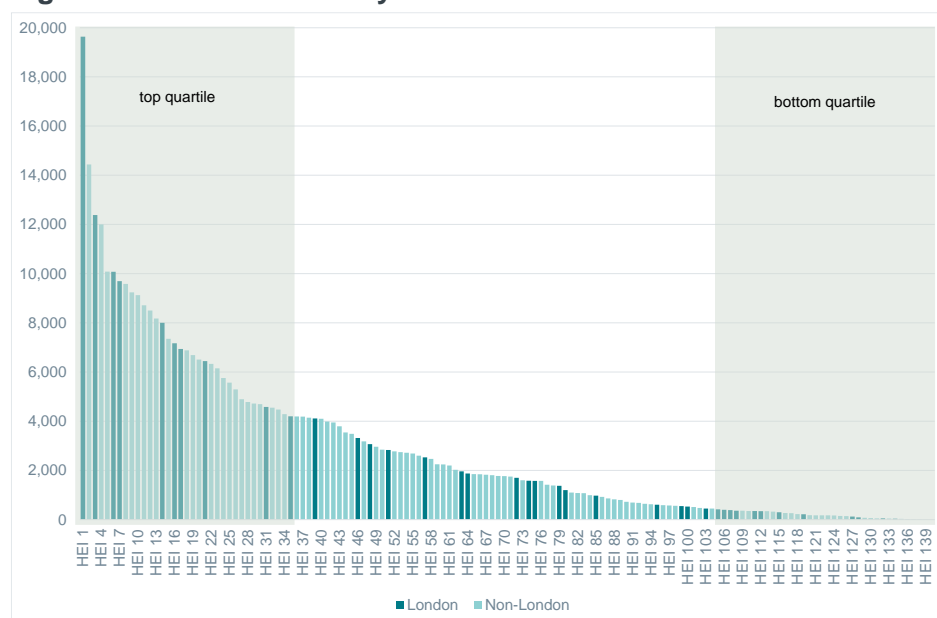
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<sup>17</sup> [https://www.hepi.ac.uk/wp-content/uploads/2020/10/Demand-for-Higher-Education-to-2035\\_HEPI-Report-134\\_FINAL.pdf](https://www.hepi.ac.uk/wp-content/uploads/2020/10/Demand-for-Higher-Education-to-2035_HEPI-Report-134_FINAL.pdf)



only five institutions account for around half of all international students in London while many have very low numbers of non-UK students (see Figure 3). Therefore, while it is true that there are certain benefits to operating in London in being able to recruit students globally, these benefits are not shared uniformly.

**Figure 3 HEIs ranked by international student intake**



Source: Frontier Economics based on HESA 2018-19 data (<https://www.hesa.ac.uk/news/16-01-2020/sb255-higher-education-student-statistics/location>)

## Conclusions

London HEIs have to take the market rates for wages and property costs and these are higher in London than the rest of the country. Removing the LW will create financial pressure for London HEIs and for those institutions which cannot absorb the shock will mean significant funding cuts elsewhere in their budgets. This can lead to lower quality of services provided to students and cause issues such as difficulties in recruitment, higher staff turnover and worsening facilities. Other policy goals such as widening participation performance may also be compromised, particularly if support for commuter students is affected.

The removal of the LW is far from being the most effective instrument for levelling up between regions. Area uplifts in funding allocations are not tools of regional or industrial policy aimed at supporting less well-off areas. There is no question that the levelling-up ambition is meritorious, but this should be encouraged through other policy levers.

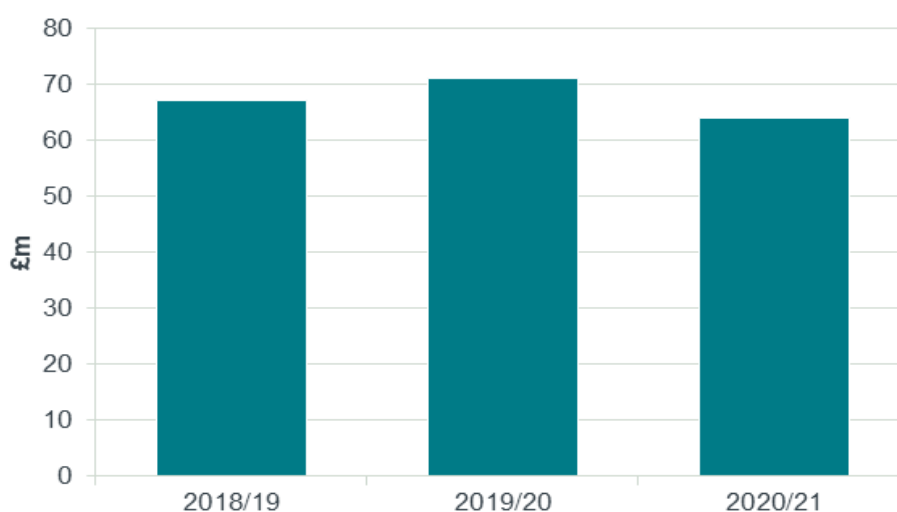
Careful consideration should be given to how the impact of a sudden funding withdrawal from London HEIs can be minimised. At a minimum, a phased approach is needed to avoid a cliff-edge scenario which will have a disproportionate impact on those London institutions who can least afford it.

## THE LONDON WEIGHTING

### What is the LW?

The LW is an uplift in funding which is there to reflect the higher cost of provision in London. The amount given for the LW varies from year to year but has been in the region of £60 to £70m for the last three academic years.

**Figure 4** Office for Students (OfS) recurrent teaching funding targeted at students attending courses in London, 2018/19 – 2020/21



Source: Office for Students, Guide to funding 2018/19, 2019/20 and 2020/21

The rates of funding for students attending courses in London depend on whether the courses are in inner or outer London. This is because the cost pressures are not the same across the whole of London, with inner London facing higher costs than outer London.

The LW is also applicable to student premiums payable to institutions to support successful student outcomes (applicable to students identified as at risk of not completing their studies). An uplift of 12% is applied for providers based in inner London and an uplift of 8% for providers in outer London.

The LW has also been included in the calculation of formula capital grants in the past although this may change in future<sup>18</sup>.

**Figure 5.** Rates of funding for students attending courses in London, 2020/21

Price group	Standard rate per FTE for inner London (£)	Standard rate per FTE for outer London (£)
A	958	599
B	407	254
C1 and C2	312	195
D	240	150

Source: Office for Students, Guide to funding 2020/21

<sup>18</sup> The OfS is currently consulting on a proposal that capital grants for providers should be allocated through a competitive bidding exercise for the 2021/22 financial year.

## Why is the LW there?

The LW has been paid to London HEIs for a long time. It is there to level the playing field as providing the same service in London is more expensive than in the rest of the country.

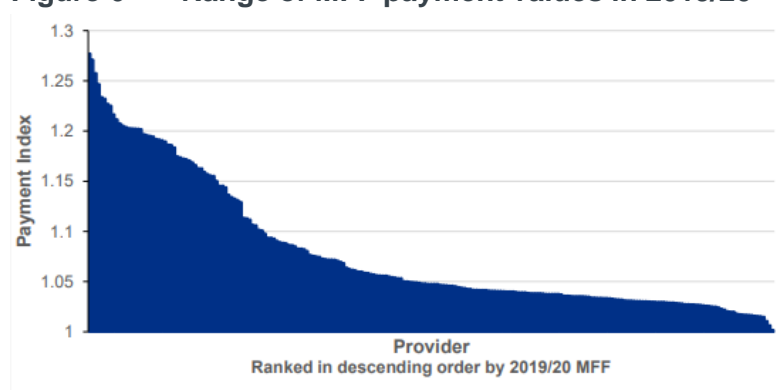
The principle is such that, in HE, if a student moves from a university in one part of the country to one in another part of the country to study the same subject (and pays the same fees), then it is expected that the quality of provision will be similar. This is similar in other contexts.

- In local government, people in different localities that pay similar levels of council tax will expect to receive a similar level of service from their respective local authorities.
- In health, where there are no charges, it is expected that levels of health services will be similar independent of where an individual lives.

Uplifts to funding are applicable in other areas of public spending. In health, for example, the market forces factor (MFF) adjustment is applied to the payments hospital trusts receive, and this reflects the higher costs of labour, land and buildings in London.<sup>19</sup> Frontier Economics' review of the MFF examined the variation in costs faced by providers of healthcare in different parts of the country by looking at staff costs (different categories of staff such as clinical and non-clinical), building and land costs, business rates and others. Our work highlighted the large variation in these costs, with the highest levels being observed in the capital.

Recognising the large variation in costs faced by healthcare providers in different parts of the country, the MFF adjustment gives an uplift in funding to London hospital trusts of more than 20% in some cases (see Figure 6).

**Figure 6** Range of MFF payment values in 2019/20



Source: NHS England and NHS Improvement, *A guide to the market forces factor*, January 2019

Note: [https://improvement.nhs.uk/documents/475/Guide to the market forces factor.pdf](https://improvement.nhs.uk/documents/475/Guide%20to%20the%20market%20forces%20factor.pdf)

There is a clear logic for compensating providers in London for the higher costs they face. Removing the LW would therefore move HE away from other areas of government spending.

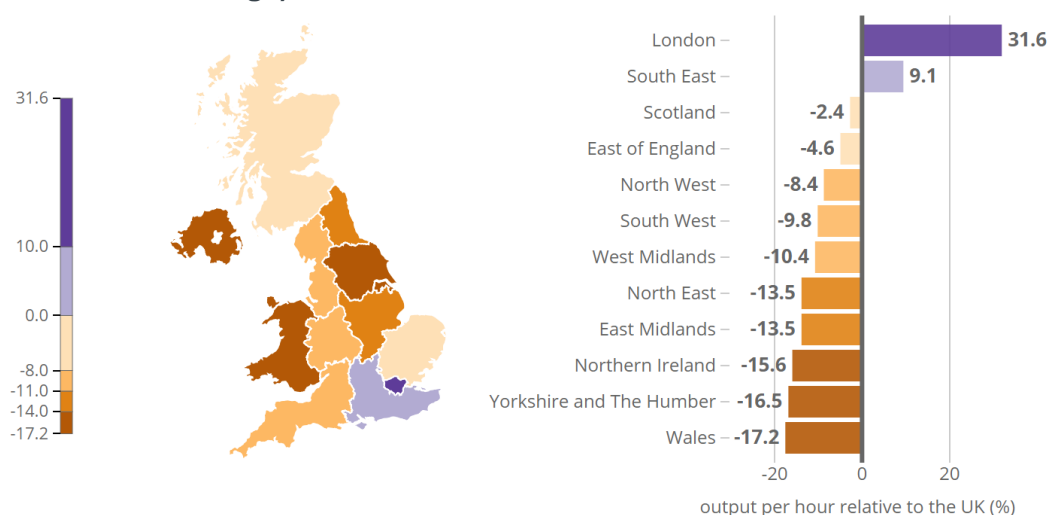
<sup>19</sup> [https://improvement.nhs.uk/documents/475/Guide to the market forces factor.pdf](https://improvement.nhs.uk/documents/475/Guide%20to%20the%20market%20forces%20factor.pdf)

# THE IMPACT OF REMOVING THE LW

## Context

London is the capital and largest city in England and the United Kingdom. It is a thriving global city with a strong economy and an increasing population (the current metro area population of London in 2021 is over 9m.<sup>20</sup> The economic success of the capital has been driven by an increasingly connected and integrated global economy. In economic terms, London is by far the most productive place in the UK (see below) and one of the most productive in Europe.<sup>21</sup>

**Figure 7 Productivity across the regions of the UK (relative to UK average)**



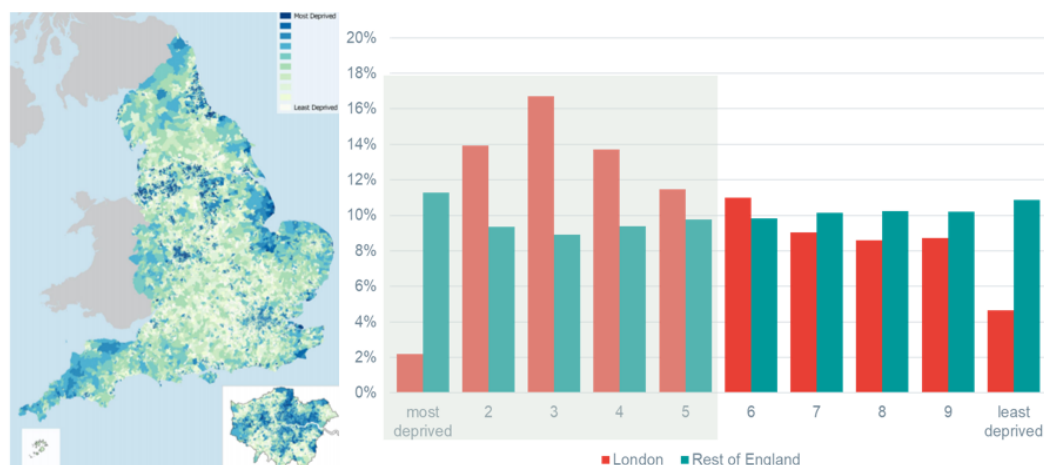
Source: Office for National Statistics<sup>22</sup>

However, there is a huge amount of variation in the economic and socio-demographic composition of different parts of London. Analysis of the 2019 Index of Multiple Deprivation (IMD) shows the significant levels of deprivation in many parts of London. In fact, although in recent years London boroughs have become relatively less deprived in comparison to other parts of the country, a third of London LSOAs are still within the top 30% of the most deprived across England.

<sup>20</sup> See: <https://www.macrotrends.net/cities/22860/london/population#:~:text=The%20metro%20area%20population%20of,a%201.45%25%20increase%20from%202018>

<sup>21</sup> See: <https://www.london.gov.uk/sites/default/files/productivity-trends-in-london-final.pdf>

<sup>22</sup> See: <https://www.ons.gov.uk/economy/economicoutputandproductivity/productivitymeasures/bulletins/regionallabourproductivityincludingindustrybyregionuk/2018#:~:text=Output%20per%20hour%20varied%20significantly,job%20followed%20a%20similar%20pattern>.

**Figure 8 Index of Multiple Deprivation (IMD)**

Source: Frontier analysis of Index of Multiple Deprivation (IMD), 2019 published by the Ministry of Housing, Communities & Local Government (MHCLG)<sup>23</sup>

Note: Proportion of Lower-layer Super Output Areas in different IMD deciles

Focusing on income alone (Income Deprivation Affecting Children Index – IDACI), eighteen London boroughs rank in the most deprived 10%. Furthermore, the income domain does not fully take account of the high rental and housing costs in London, and therefore may underestimate the levels of deprivation in the capital.<sup>24</sup>

Income and wealth inequality are also particularly stark in London, with the top decile earning ten times as much as the bottom decile.

## HE provision in London

London is home to a diverse set of HE providers. There are 39 HEIs<sup>25</sup> in London, ranging from global institutions ranking in the top 20 in the world (such as Imperial College London and University College London)<sup>26</sup> through to lower-ranking, teaching-focussed institutions which primarily educate local students.

According to HESA data, in the 2018/19 academic year, London HEIs had ca. 385,000 student enrolments, representing around a fifth of the total for England. The student base for London universities is extremely diverse. In 2018/19, there were:

- 122,000 enrolments by international students (ca. 30% of the total for England); and
- 117,000 enrolments by UK-domiciled Black, Asian and minority ethnic (BAME) students (30% of total).

<sup>23</sup> <https://www.gov.uk/government/statistics/english-indices-of-deprivation-2019>

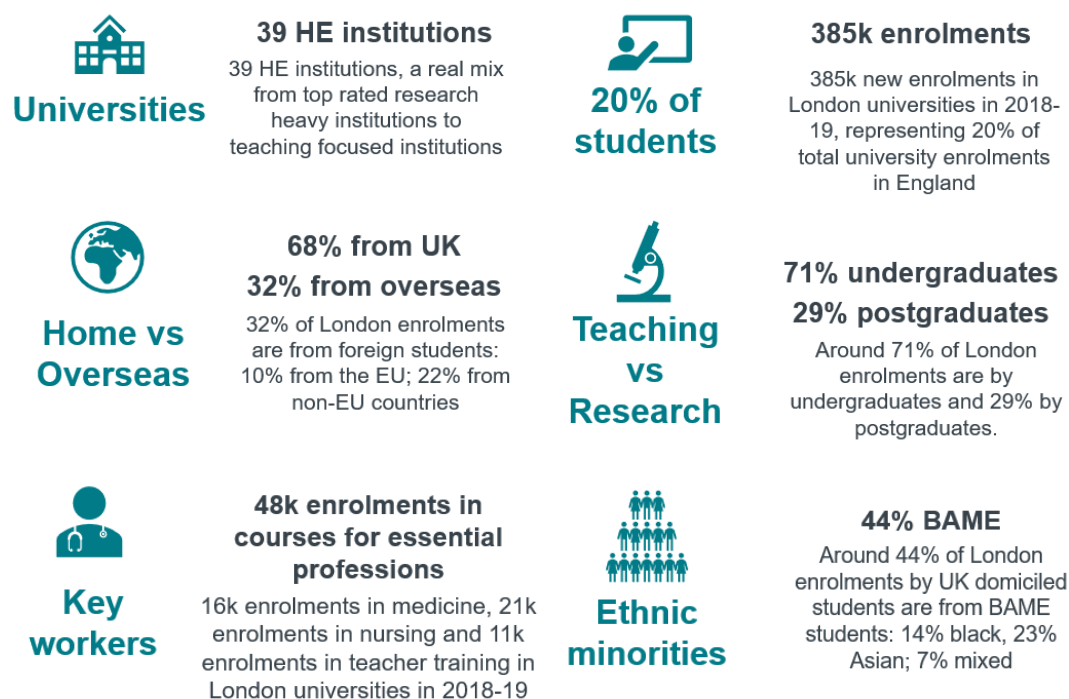
<sup>24</sup> <https://www.londoncouncils.gov.uk/members-area/member-briefings/local-government-finance/indices-deprivation-2019#:~:text=London%20is%20comparatively%20less%20deprived,per%20cent%20most%20deprived%20nationally.>

<sup>25</sup> Excluding universities primarily located elsewhere in the country which have a small London presence.

<sup>26</sup> [https://www.timeshighereducation.com/world-university-rankings/2021/world-ranking#!/page/0/length/25/sort\\_by/rank/sort\\_order/asc/cols/stats](https://www.timeshighereducation.com/world-university-rankings/2021/world-ranking#!/page/0/length/25/sort_by/rank/sort_order/asc/cols/stats)

London HEIs educate a significant proportion of **key workers**: in 2018-19 there were ca.16,000 enrolments in medicine, 21,000 enrolments in nursing and 11,000 enrolments in teacher training.<sup>27</sup>

**Figure 9 London HE provision**



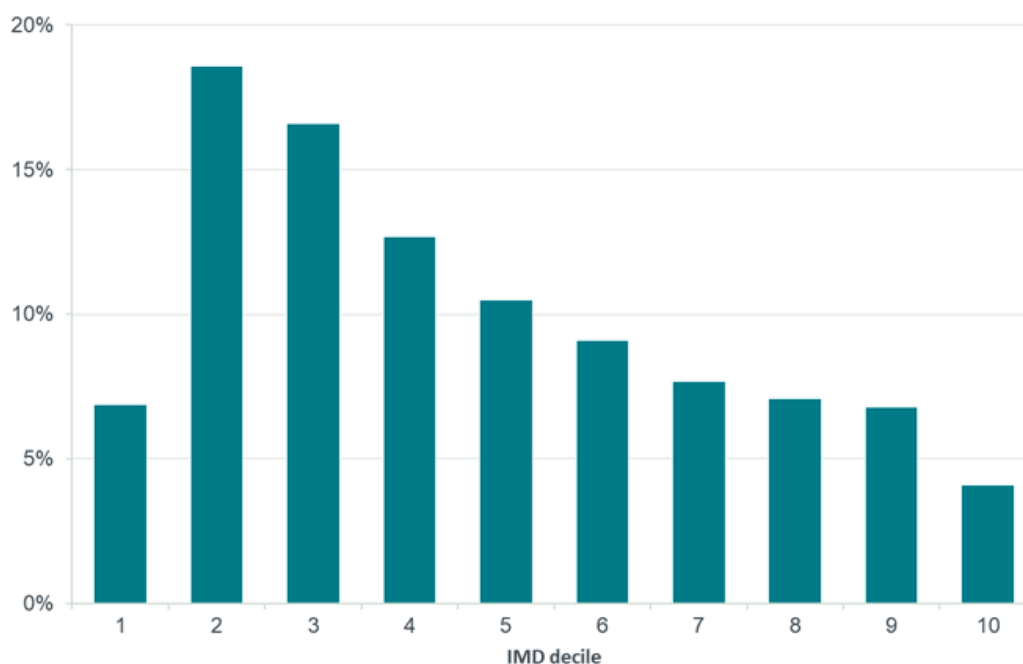
Source: Frontier Economics analysis of HESA data

Note: Data for 2018-19

The levels of economic disadvantage in London highlighted in the previous section are reflected in the student intake at London universities. Figure 10 shows the percentage of young Londoners entering HE, broken down by levels of deprivation (as measured by the IMD). It is evident that a significant fraction of young people in relatively less well-off areas are entering HE – around a quarter of HE entrants are from the bottom two deciles, i.e. the areas with the highest levels of deprivation.

<sup>27</sup> HESA data on higher education student enrolments by HE provider and subject of study relative to academic year 2018/19.

**Figure 10** Percentage of young London entrants into HE by IMD deciles (2018/19)



Source: *The HE journey of young London residents, London Councils*<sup>28</sup>

Our conversations with senior leadership teams at various institutions confirmed that a large proportion of their students are local and from disadvantaged backgrounds:

*“The large majority of our students are from London; and the great majority are commuter students. These are students who cannot afford other universities. They’re commuting because they have no choice. They can’t afford to live on campus.”*, Senior Leader of a London HEI

*“We’re talking about under-privileged students, many are commuter students. They need more input, and more support, not less.”*, Senior Leader of a London HEI

Indeed, recent research has highlighted that students from the lowest socio-economic groups are more likely to stay at their homes, rather than move closer to their place of study<sup>29</sup>.

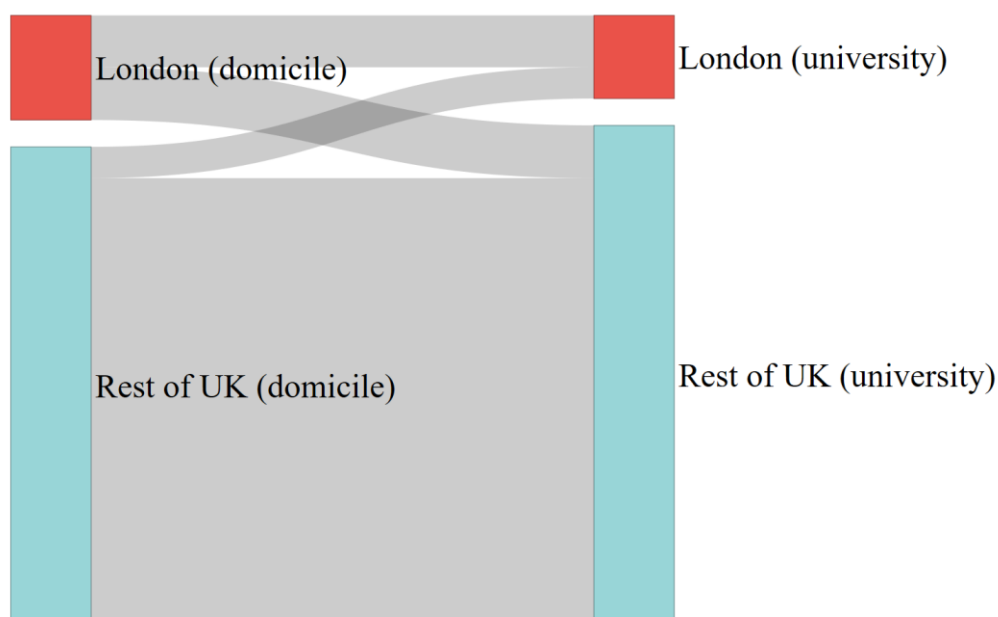
It is indeed the case that a significant proportion of Londoners (around half) pursuing HE do so in the capital (see Figure 11)<sup>30</sup>.

<sup>28</sup> <https://www.londoncouncils.gov.uk/higher-education-journey-young-london-residents-2018>

<sup>29</sup> Donnelly, M. and Gramsu, S. (2018) *Home and Away: Social, Ethnic and Spatial Inequalities in Student Mobility*, London: Sutton Trust. Available at: [https://www.suttontrust.com/wp-content/uploads/2019/12/Home\\_and\\_away\\_FINAL.pdf](https://www.suttontrust.com/wp-content/uploads/2019/12/Home_and_away_FINAL.pdf)

<sup>30</sup> This data is not available at HEI level but our understanding from conversations with London HEI senior leaders suggest that London HEIs with a teaching focus are more likely to draw students from the local area.

**Figure 11 HE student enrolments by domicile and region of HE provider – academic year 2019/20**



Source: Frontier Economics analysis of HESA data

## Costs of HE provision in London

London HEIs have to spend more on staff, buildings and other costs as input prices are higher in London than in the rest of the country. Due to increased property costs, many HEIs in the capital own the lease rather than the freehold on estates.

The largest component of operating costs for HEIs is staff costs. This represents around 55% of HEI expenditure, on average.<sup>31</sup> London HEIs are contractually obliged to pay a London allowance to many of their staff. The exact amount of this allowance varies from institution to institution but is typically in excess of £3,000 per member of academic staff (FTE). The latest HESA data shows that London HEIs employ around 45,000 academic staff (27,000 full-time and 18,000 part-time staff). The London allowance applied to full-time *academic* staff alone (not including part-time staff) therefore is likely to add at least £80m to staff costs for London HEIs – an amount which easily exceeds the £64m received in LW.

Of course, the reality is that non-academic staff (ca. 35,000) are also paid more compared to similar jobs outside London, as dictated by market forces. Analysis of the latest Annual Survey of Hours and Earnings (ASHE) data<sup>32</sup> shows that median wages in London<sup>33</sup> are more than 20% higher than in the rest of the UK (see Figure 12).

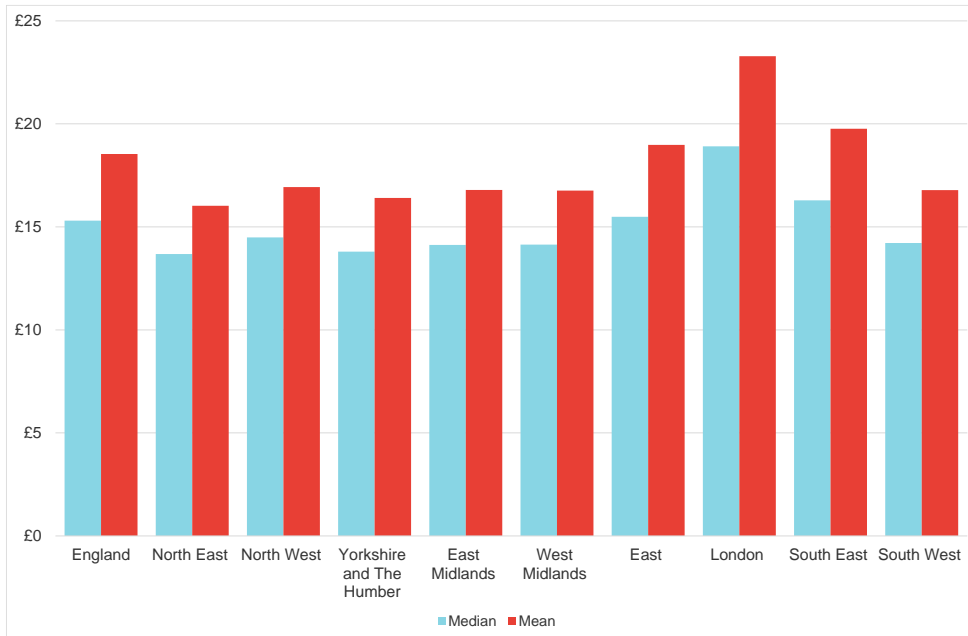
<sup>31</sup> Calculated as the average share of staff costs over total operating costs over the period from 2015/16 to 2018/19.

<sup>32</sup> <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/regionalbyindustry2digitsicashetable5>

<sup>33</sup> Full-time gross hourly pay across all industries and occupations.



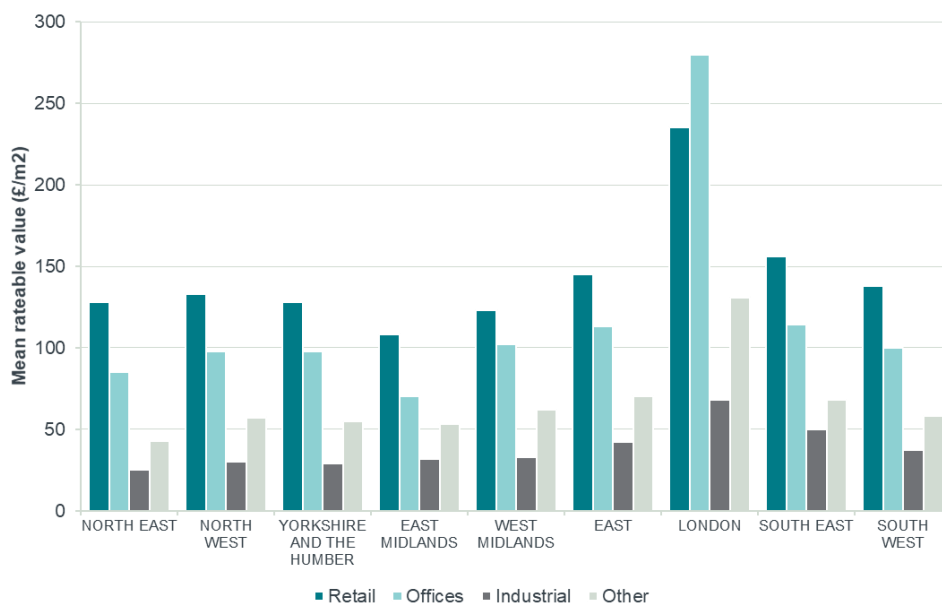
**Figure 12** Gross hourly pay: full-time employees



Source: Frontier Economics analysis of ASHE 2020 data

The differences in unit costs can be even more pronounced when it comes to other inputs such as land and buildings. Analysis conducted by the Centre for Cities based on Valuation Office Agency data shows that median rateable value per square metre in the capital is more than double the median value for England and Wales.<sup>34</sup> This point is also demonstrated in Figure 13.

**Figure 13** Rateable values (per square metre) for commercial land use across England and Wales



Source: Valuation Office Agency

Note: Data for 2012

<sup>34</sup> <https://www.centreforcities.org/reader/city-space-race-balancing-need-homes-offices-cities/geography-demand-residential-commercial-space/>

As is the case with staff costs, the cost of land and rents (per unit) is determined by market forces outside the control of universities, and these add significantly to the total expenditure of London HEIs.

The cost differences between London and the rest of the country have been well documented in previous research acknowledged in the OfS consultation on recurrent funding for 2021-22<sup>35</sup>. For example, research by Deloitte<sup>36</sup> for the Higher Education Funding Council for England (HEFCE) found that average academic staff costs in London were around 12-14% higher than the national average with the difference even more pronounced for non-academic staff costs. Recent KPMG<sup>37</sup> work has also found that provision in London is more costly relating to both academic and non-academic staff costs and also to land, building and maintenance costs.

Our conversations with senior leaders at London universities highlighted the significantly higher costs they face:

*“The LW is important as most things in London cost more. I have worked at other universities outside London for over 20 years and there is no comparison in terms of costs. Staff are paid more and leasing buildings is extremely expensive with rates per square metre constantly increasing.”, Senior Leader of a London HEI*

*“The University is still required to pay out a London Weighting on their staff wage bill, which increases each year in alignment with the pay award. This is putting the University at a cost disadvantage in its ability to provide the same level of student experience to universities based outside of London.”, Senior Leader of a London HEI*

Hence, the removal of the LW will create an **uneven playing field** (in terms of unit costs) by requiring London universities to absorb the consequences of being located in a conurbation with higher unavoidable costs.

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<sup>35</sup> <https://www.officeforstudents.org.uk/media/8610a7a4-0ae3-47d3-9129-f234e086c43c/consultation-on-funding-for-ay2021-22-finalforweb.pdf>

<sup>36</sup> <https://webarchive.nationalarchives.gov.uk/20180405115447/http://www.hefce.ac.uk/pubs/rereports/year/2017/regional/>

<sup>37</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/909349/Understanding\\_costs\\_of\\_undergraduate\\_provision\\_in\\_higher\\_education.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/909349/Understanding_costs_of_undergraduate_provision_in_higher_education.pdf)

## CASE STUDY 1

### Context

University A is a relatively small, rapidly growing institution which primarily focuses on teaching undergraduate courses. It aspires to also expand its research over time, but research currently makes up only a small fraction of its activities.

The majority of its students are from the UK and are local – approximately 60% of its undergraduate students are from within a 20-mile radius of the university. It has sizeable BAME and mature student populations – both categories make up around 40% of undergraduates. A lot of their students are from disadvantaged backgrounds and often require support in order to remain in education.

### State of finances

Last year (FY2019/20) University A managed to break even, just. Most of its income comes from home students and, while costs have been increasing steadily in line with inflation, tuition fees have been frozen at £9,250 for a couple of years now. This is pushing them closer and closer to a deficit.

*“The LW is important as most things in London cost more. I have worked at other universities outside London for over 20 years and there is no comparison in terms of costs. Staff are paid more and leasing buildings is extremely expensive with rates per square metre constantly increasing. Unlike some of the top institutions we don’t have endowment income and our ability to generate extra income is extremely limited.”*

### Impact of LW withdrawal

Despite the additional costs from managing within the pandemic, University A is still projecting to break even this year. However, removing the LW would immediately push it into deficit and would do that quite drastically.

*“For us this is the difference between remaining afloat or not. Losing the LW would be disastrous and I can’t believe the government would want that.”*

*“We rely on tuition fee income and we have no other significant sources of funding which we could use to plug the gap. We would like to attract more international students but this requires investment and time.”*

*“So, the only thing we can do is to cut costs which in practice means jobs. At current rates, this would mean up to twelve teaching jobs, which equates to one in ten of our academic staff.”*

*“These students are local, many of them commuter students. If we close these courses down, they will likely drop out from HE.”*

## The impact of LW removal on universities

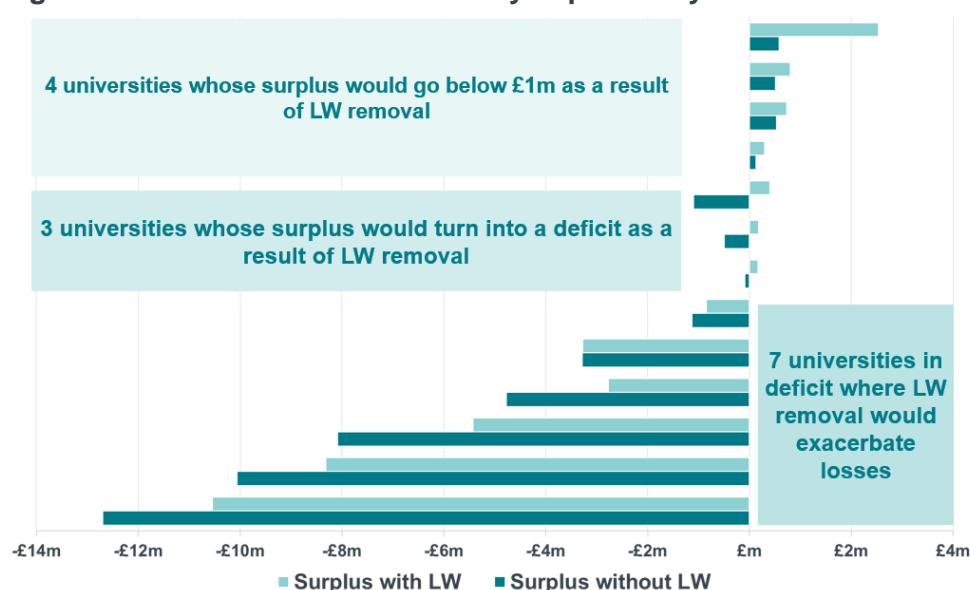
Removing LW from the SPG will have a significant negative impact on London HEIs' finances, with some groups being disproportionately affected.

### A subset of institutions are particularly vulnerable to this funding cut

The removal of the LW element of the SPG would result in a funding shortfall for London HEIs of around £64m, or a 13.7% reduction in mean SPG<sup>38</sup> although the net reduction in funding (accounting for the redistribution of other grants) is likely to be just under £50m according to the OfS<sup>39</sup>. Removing this funding would create additional substantial financial pressure for London universities and impact their viability at a time when the sector is emerging from a global pandemic and other major policy changes such as Brexit – both are associated with significant risks for student recruitment, particularly international students. All universities receiving LW funding will be affected by this proposal as the amounts of funding received are not trivial. However, given the significant variation in financial performance across institutions, it is likely that a number will be hit particularly hard:

- 7 universities which are already making losses will have current losses significantly exacerbated;
- 3 universities will go from making a surplus to being in deficit; and
- 4 universities will have their surpluses reduced to £1m or less.

**Figure 14 Universities most heavily impacted by LW removal**



Source: HESA data FY2018/19.

Note: Figures for FY2018/19 are adjusted to account for the 2017 USS pension scheme revaluation, as this expense is not a typical annual operating expense. Chart shows universities most affected by the LW withdrawal<sup>40</sup> but one with particularly high losses has been excluded to improve readability.

<sup>38</sup> <https://www.officeforstudents.org.uk/media/a3814453-4c28-404a-bf76-490183867d9a/rt-hon-gavin-williamson-cbe-mp-t-grant-ofs-chair-smb.pdf>

<sup>39</sup> <https://www.officeforstudents.org.uk/media/8610a7a4-0ae3-47d3-9129-f234e086c43c/consultation-on-funding-for-ay2021-22-finalforweb.pdf>, Paragraph 46.

<sup>40</sup> We estimate that the remaining 24 London universities will have surpluses cut back by 8.5% on average.

## CASE STUDY 2

### Context

University B is a specialist institution. More than 80% of its students are undergraduates and many of them are on a long programme. The majority of its students are from the UK and a large majority are local. Most students do not live in halls of residence. University B trains essential workers who fill strategic positions within sectors with considerable shortages exacerbated by the current crisis.

### State of finances

Because of the effect of COVID-19, in the last year (FY2019/20) University B reported a deficit. Most of University B's income comes from home students, whose number is unlikely to increase as most of its courses have a fixed number of places. Therefore, University B does not have any leverage to compensate for the removal of the LW except by cutting costs:

*“Our financial resilience would be undermined. Our only option would be to cut staff costs and remove student enrichment opportunities and enhancement projects”*

### Impact of LW withdrawal

University B is projecting a small surplus this year. Removing the LW would immediately push it into deficit. University B is concerned that this would result in job losses and in the elimination or reduction of student enrichment activities, with a consequent negative impact on the student experience:

*“Some of our healthcare courses are of strategic importance for the NHS as they train workers in essential professions where there are workforce shortages. These courses can be loss making and difficult to recruit for.”*

University B has to invest significant amounts of money in consumables and equipment to facilitate an education enhanced by hands-on experience. These have to be upgraded continuously in order to remain relevant and so that the healthcare professionals the university trains can use the latest technology which is used in hospitals around the country.

*“Some of our courses are small although they are very important for the NHS given the current levels of staff shortages. They tend to recruit small numbers of students but require equipment and simulation facilities for practical and experiential learning that are very expensive to run. In some cases these can be loss making courses but we provide them for their strategic importance!”*

University B is very constrained in its ability to generate income from other sources given that home undergraduate tuition fees have been frozen and its student numbers are capped. As such, if the LW were removed, its only option would be to cut costs, which would ultimately have an impact on students.

*“This would mean cutting academic staff, and reducing support schemes for students, like mental health support, learning development, career service and many other enrichment and engagement opportunities. This would impact the quality of our provision to our students and would negatively affect their mental health and employability.”*

### **HEIs with a teaching focus which train key workers and play an important role in widening participation in HE will be particularly affected**

Universities which focus on teaching are likely to be disproportionately affected – these often train **key workers such as teachers, social care workers and medical staff** (professions where London has historically had low retention, typically owing to the high costs of accommodation). Such institutions tend to rely on tuition fee income from home undergraduate students (often commuter students) where tuition fees have been frozen for a few years and so revenue is difficult to increase despite costs continuing to rise. Some courses are loss making (undersubscribed and with low student numbers) but are provided because they feed into **shortage occupations for the NHS** – removing funding makes these types of courses even less viable.

*“Some of our healthcare courses are of strategic importance for the NHS as they train workers in essential professions where there are workforce shortages. These courses can be loss making and difficult to recruit for.”* Senior Leader of a London HEI

*“Some of our courses are small although they are very important for the NHS given the current levels of staff shortages. They tend to recruit small numbers of students but require equipment and simulation facilities for practical and experiential learning that are very expensive to run. In some cases these can be loss making courses but we provide them for their strategic importance!”*, Senior Leader of a London HEI

Therefore, one unintended consequence of the LW removal is likely to be an aggravation of the supply shortage of key workers in London’s labour market. This comes at a time when COVID-19 is putting unprecedented pressure on people working in adult social care. London registered a staff turnover rate of 27.5% in 2018/19. Among those who left their roles in 2018/19, the proportion of those who stayed in adult social care was considerably lower in London (32%) than in any other region.<sup>41</sup>

It is also the case that staff shortages within the NHS are distributed unevenly across the country, with the highest percentage of FTE vacancies in London (10.7%).<sup>42</sup> Despite the opportunities that London’s education system offers, it faces a significant and growing teacher supply challenge as it struggles to retain teachers over the long term. London’s schools will need more teachers over the next few years as pupil numbers are forecast to grow rapidly, especially at secondary level. London already has more new entrants to its teacher workforce each year, driven by a greater proportion of newly qualified teachers than in other large cities and the rest of England. But these new teachers may not be enough to replace the many teachers who leave London each year.<sup>43</sup>

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<sup>41</sup> <https://www.health.org.uk/news-and-comment/charts-and-infographics/even-before-covid-19-high-workforce-turnover-rates-posed-a>

<sup>42</sup> <https://www.nuffieldtrust.org.uk/resource/the-nhs-workforce-in-numbers>

<sup>43</sup> [https://www.london.gov.uk/sites/default/files/nfer\\_gla\\_teacher\\_supply\\_retention\\_and\\_mobility\\_in\\_london\\_2018\\_0.pdf](https://www.london.gov.uk/sites/default/files/nfer_gla_teacher_supply_retention_and_mobility_in_london_2018_0.pdf)

### CASE STUDY 3

#### Context

University C is a medium-sized institution. The university focuses on teaching undergraduate courses with a particular focus on professions which can be categorised as 'key workers'. It also has a significant postgraduate and research portfolio. The university has a very significant proportion of BAME students (ca. 50% of students) and those from lower-income backgrounds. Students also tend to be slightly older and the majority commute from within London:

*"The large majority of our students are from London; and the great majority are commuter students. These are students who cannot afford other universities. They're commuting because they have no choice. They can't afford to live on campus."*

#### State of finances

The financial position of University C is very challenging. Last year (FY2019/20) University C made a sizeable loss and it is expecting to make a loss again this year (2020/21). This is driven by a range of factors including reductions in income as a result of the pandemic.

#### Impact of LW withdrawal

Removing the LW would dramatically worsen the financial position of the institution at a time when other risks (e.g. COVID-19, Brexit) are already having a significant impact. University C is concerned that the removal of funding will result in job losses:

*"We would try as hard as we can to reduce other costs, but energy, rent etc. cannot be cut and we have already reduced costs during the pandemic. It's most likely we would need to reduce staff expenditure. That would reduce what we can provide in terms of support to students."*

This would impact its disadvantaged students many of whom are training to be key workers:

*"This will most penalise universities which can least afford it. And it's taking away capacity that is primarily being accessed by under-privileged students, many of whom are training to become key workers."*

*"We're talking about under-privileged students, many are commuter students. They need more input, and more support, not less."*

As such, the impacts of this would be felt beyond London as many of the key workers move out of London for work after graduating. The decision to remove the LW has come very suddenly and does not provide the university with sufficient time to plan appropriately:

*"This would represent a permanent recurrent reduction in income. That takes longer than a year to plan for. Especially as we emerge from one of the most challenging times in our history from a finance point of view."*

London’s universities will have an important role to play in providing the additional supply of essential workers needed in London. As Figure 15 shows, at present nearly half of UK-domiciled HE leavers working in London were trained in London universities and as noted previously a significant proportion of key workers are trained in London.

**Figure 15 UK-domiciled HE leavers in work in the UK, by region of domicile, region of HE provider and region of employment – 2016/17**



Source: Frontier Economics analysis of HESA data

The most vulnerable institutions train high numbers of local students from difficult and disadvantaged backgrounds who require significant support to complete their education. Removing funding from these may harm other policy objectives such as **widening participation**.

*“This will most penalise universities which can least afford it. And it's taking away capacity that is primarily being accessed by under-privileged students.”, Senior Leader of a London HEI*

*“The large majority of our students are from London; and the great majority are commuter students. These are students who cannot afford other universities. They're commuting because they have no choice. They can't afford to live on campus.”, Senior Leader of a London HEI*



## CASE STUDY 4

### Context

University D is a top ranking institution. It is one of the best performing universities in the country for research quality. The majority of students at University D are from overseas. Almost half of its student population are studying at postgraduate level and around a third are BAME.

### State of finances

Last year (FY2019/20) University D reported a surplus, although this fell substantially as a result of COVID-19. In FY2020/21 University D expects to report a substantial operating loss. This is due to significant revenue falls from various activities and increases in expenditure – for example, it had to refund students who left their accommodation and moved to online teaching. In addition to this, it spent a significant amount of money to make the campus safe and to set up testing infrastructure.

Revenue from ancillary activities is important as teaching and research activities just about break even. Furthermore, its revenues heavily depend on tuition fees from foreign students. Therefore, it is facing significant risks given the uncertainties around international travel restrictions due to the global pandemic.

### Impact of LW withdrawal

University D is expecting to report a small surplus in the next year. Moreover, as its revenue heavily depends on foreign students tuition fees, it is facing significant risks as a result of Brexit and COVID-19. Consequently, LW removal could affect its budget planning with a negative impact on staff recruitment and students' experience:

*“The reduction in income resulting from the LW withdrawal would put downward pressure on the amount of staff that we are able to hire and the amount of support we are able to deliver to students.”*

*“Given all the risks we are facing right now, this would potentially delay investment and expenditure, threaten student experience and limit research capacity.”*

*“There is a lot of evidence that, when compared to other universities, London institutions are always skewed towards higher costs. The decision of removing LW seems to us a very destabilising signal.”*

### Removing funding at short notice will have an impact on students

Removing significant funding at such short notice will leave universities with few options for absorbing the shock. Many have no cushion to fall back on so will have to cut costs, which in practice means cutting staff as other costs are harder to control in the short term.

*“If you need to find money, you have four options: (1) Reduce the size of your surplus – we have none; (2) Increase your income – we have no way to do this immediately; (3) Increase borrowing – we have reached the limits of what we can borrow; (4) Cut costs.”, Senior Leader of a London HEI*

*“We would try as hard as we can to reduce other costs, but energy, rent etc. cannot be cut and we have already reduced costs during the pandemic. It’s most likely we would need to reduce staff expenditure. That would reduce what we can provide in terms of support to students.”, Senior Leader of a London HEI*

Reducing staff costs will mean reducing pay, where possible, or reducing headcount or some combination of both. Both have an impact on staff morale and the quality of service provided, and both could jeopardise the provision of student support services and enrichment activities, thus **negatively affecting the student experience** (especially for disadvantaged students who rely more on support services). These points were made by a number of senior leaders at London universities whom we interviewed:

*“Less money simply means less spend per student. We will have less to spend on the student experience as we’d be forced to reduce spend on things like staffing levels, capital projects, facilities and so on. In the end these things affect the student experience.”, Senior Leader of a London HEI*

*“So, the only thing we can do is to cut costs which in practice means jobs. At current rates, this would mean tens of teaching jobs.... These students are local, many of them commuter students. If we close these courses down, they will likely drop out from HE.”, Senior Leader of a London HEI*

*“Our financial resilience would be undermined. Our only option would be to cut staff costs and remove student enrichment opportunities and enhancement projects.”, Senior Leader of a London HEI*

*“This would mean cutting academic staff, and reducing support schemes for students, like mental health support, learning development, career service and many other enrichment and engagement opportunities. This would impact the quality of our provision to our students and would negatively affect their mental health and employability.”, Senior Leader of a London HEI*

## CASE STUDY 5

### Context

University E is a post-1992 institution offering a wide subject range with a vocational focus. It is ranked in the top 100 among UK universities. Around 70% of its students are undergraduates. More than three-quarters are from the UK and a majority (>50%) are commuter students. University E has sizeable BAME (>50%) and mature student populations (>35%). The university plays an important role in the widening participation agenda, drawing from a very disadvantaged demographic (more than half of students come from the ca. 40% of the most deprived areas in the country).

### State of finances

University E has made a surplus in the last three years, although the environment has become very challenging – significant accommodation rebates (worth several million pounds) have had to be paid out due to the COVID-19 pandemic. The university has strong controls on discretionary spend, which has helped it to maintain a surplus, but some costs are beyond its control, such as the London supplement which is payable to staff (worth more than £4,000 per academic staff member) and the impact of pension scheme revaluation on employer contributions.

### Impact of LW withdrawal

University E is projecting a surplus this year but removing the LW would immediately halve the level of that surplus. This is yet another cost shock which the university will have to absorb, and something will have to give.

*“The University is still required to pay out a London Weighting on their staff wage bill, which increases each year in alignment with the pay award. This is putting the University at a cost disadvantage in its ability to provide the same level of student experience to Universities based outside of London.”*

*“We are trying to continue to grow student numbers and exploit economies of scale as income per head is fixed and yet our cost base is exposed to inflationary pressure. But this is a challenging and competitive market and growing numbers is not easy.”*

In the end, the university is concerned that if it is not able to grow student numbers to make up for the drop in funding, then the student experience will be impacted.

*“Less money simply means less spend per student. We will have less to spend on the student experience as we’d be forced to reduce spend on things like staffing levels, capital projects, facilities and so on. In the end these things affect the student experience. The impact on student experience falls disproportionately on students from deprived areas because we have a higher weighting of these students at our University relative to other Universities”*

Reductions in surpluses will affect the ability of the university to reinvest and sustain the level of service and facilities students should expect from their tuition fee.

*“We need a surplus in order to finance capital projects and other investments which ultimately mean that we can remain competitive and provide a good experience for our students. Reducing funding will clearly have a negative impact on that.”*

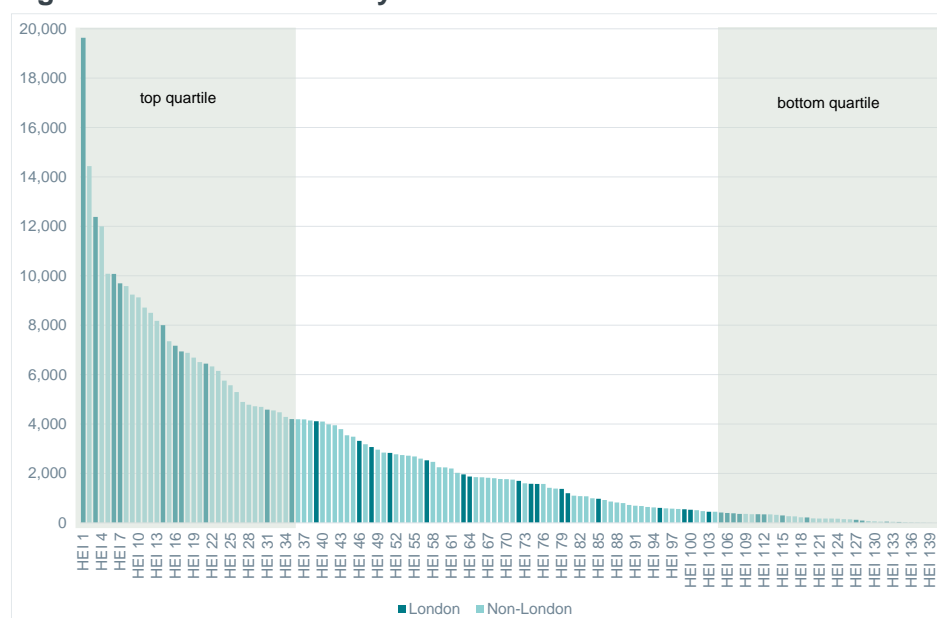
### Levelling down London is not the way to level up the regions

There is a strategic policy initiative to level up the regions in the UK and the education sector will play an important role in this. However, for all the reasons described above, taking funds away from London’s HEIs risks undermining the notion of a level playing field that the LW seeks to provide and, instead, will put London’s HEIs at a significant funding disadvantage compared to other HEIs elsewhere in the country. Some London HEIs, particularly those with a teaching focus and a relatively small international student intake will be disproportionately affected.

Taking away funds from London HEIs and spreading them across the country, potentially to areas and providers which are already relatively well off, is unlikely to help achieve the levelling-up policy goal. Particularly when many London institutions are already in deficit and domestic demand for HE in the capital is set to rise by 2035, with many ‘first generation’ students who are unlikely to move elsewhere pursuing a higher education.<sup>44</sup>

It is true that London is a major destination for international students accounting for around 30% of the England total. This clearly benefits local institutions and the economy. However, international students are not evenly distributed among London HEIs – only five institutions account for around half of all international students in London while many have very low numbers of non-UK students (see Figure 16) indicating that their ability to generate income from other sources in order to compensate for the LW removal is limited. Therefore, while it is true that there are certain benefits to operating in London in being able to recruit students globally, these benefits are not shared uniformly.

**Figure 16 HEIs ranked by international student intake**



Source: Frontier Economics based on HESA 2018-19 data (<https://www.hesa.ac.uk/news/16-01-2020/sb255-higher-education-student-statistics/location>)

<sup>44</sup> [https://www.hepi.ac.uk/wp-content/uploads/2020/10/Demand-for-Higher-Education-to-2035\\_HEPI-Report-134\\_FINAL.pdf](https://www.hepi.ac.uk/wp-content/uploads/2020/10/Demand-for-Higher-Education-to-2035_HEPI-Report-134_FINAL.pdf)

## CONCLUSIONS

London HEIs have to take the market rates for wages and property costs and these are higher in London than the rest of the country. Removing the LW will create financial pressure for London HEIs and for those institutions which cannot absorb the shock will mean significant funding cuts elsewhere in their budgets. This can lead to lower quality of services provided to students and cause issues such as difficulties in recruitment, higher staff turnover and worsening facilities. Other policy goals such as widening participation performance may also be compromised, particularly if support for commuter students is affected.

The removal of the LW is far from being the most effective instrument for levelling up between regions. Area uplifts in funding allocations are not tools of regional or industrial policy aimed at supporting less well-off areas. There is no question that the levelling-up ambition is meritorious, but this should be encouraged through other policy levers.

Careful consideration should be given to how the impact of a sudden funding withdrawal from London HEIs can be minimised. At a minimum, a phased approach is needed to avoid a cliff-edge scenario which will have a disproportionate impact on those London institutions who can least afford it.

