Paying for higher education

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*University financing has again emerged as a key battleground issue. Should fees be regulated lower and if so, how will the cost be financed? **Gill Wyness** explores these questions.*

The UK has dramatically increased the supply of graduates over the last four decades. The proportion of workers with higher education has risen from only 4.7 per cent in 1979 to 28.5 per cent in 2011. Rather than this enormous increase in supply reducing the value of a degree, the pay of graduates relative to non-graduates has risen over the same period: from 39 per cent to 56 per cent for men and from 52 per cent to 59 per cent for women. This implies a strong and continuing employer demand for education.

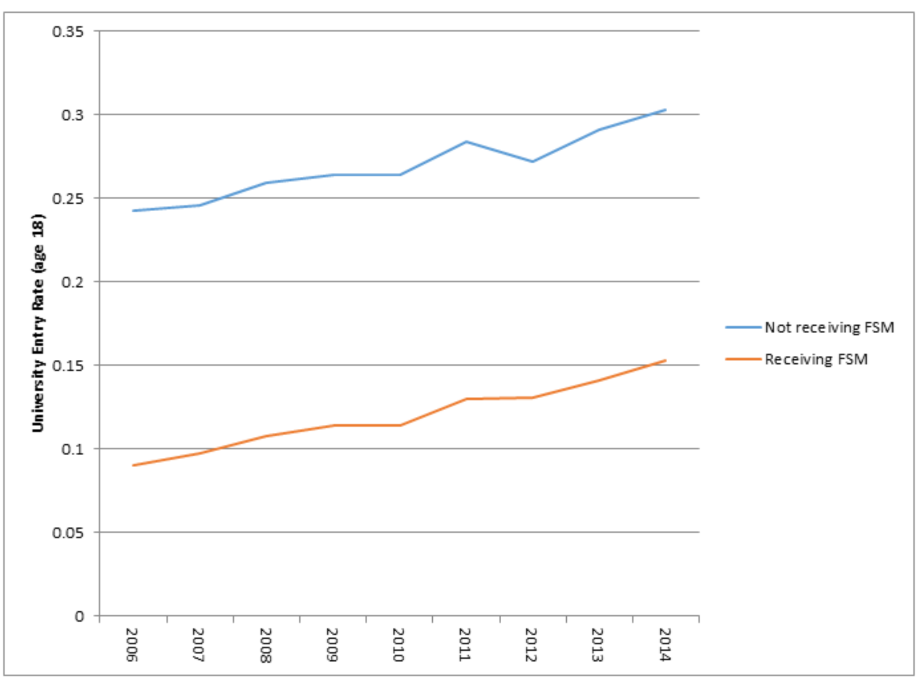
The expansion of universities helped raise growth and productivity, but placed a strain on government finances since universities receive government funding for every UK/EU student they teach, and students receive government funding in the form of loans and grants.

To help address this, the tuition fee cap was increased from £3,375 to £9,000 per year in 2012. The fee increase was accompanied by large cuts to university funding. The idea was to transfer the burden of the cost of higher education from the taxpayer to graduates and to make the system more competitive: it was expected that only the top universities would charge the full £9,000 per year, while the others could compete on price as well as quality.

Students from low income families are protected by a combination of more generous maintenance grants for the very poor, and by the fact that tuition fees are covered by a loan that would not have to be paid until the student graduated and earned more than the median wage of £21,000.

Nevertheless, there were widespread fears that participation in higher education would plummet as a result of the fee increase, and that those from poor backgrounds would be frozen out of university. But in fact, participation continued to grow and participation rates among poor students have grown at a faster rate than richer students since 2012 (see figure 1).

Figure 1: Participation in UK universities (UCAS)



***Source*: UCAS 2014.**
***Notes*: Entry rates for English 18 year old state school pupils by free school meal (FSM) status at age 15.**

This is somewhat reassuring as it implies that university access hasn't been damaged by the increase in costs. But inequality in HE remains widespread: only 15.3 per cent of disadvantaged pupils who were eligible for free school meals applied to university in 2014 (up from 13 per cent before the fee increase), compared with just over 30 per cent of those who were not eligible. It is hard to know for sure what would have happened to participation growth in the absence of £9,000 fees, but there is no clear change in trend after fee introduction. And of course, much of the inequality arises from the fact that the A-level attainment of disadvantaged young people is far lower than those from better off backgrounds, making them less likely to be accepted to university – implying tuition fees are not behind the low participation rates of disadvantaged students.

While they may not have harmed access, the tuition fee reforms have been widely criticised for failing to deliver the savings the government hoped for. This is partly because fee and maintenance loan repayment terms are still very generous under the new system. Though an interest rate has been added, the repayment threshold and length of the loan have been increased. And because loans are even bigger than before (driven by the increase in tuition fees), even more money will remain unpaid and have to be covered by the taxpayer. Recent projections suggest that around three quarters of students will not repay their government-backed student loans in full.

The upshot is that increasing fees to £9,000 per year actually cost the taxpayer money. It is only after taking account of the large cuts in the universities teaching grant – which saw many courses losing funding altogether – that the government will eventually make a saving – of around £760 million on the previous system.

The reforms also failed to deliver a more market based sector: there is almost no variation in tuition fees, with the average fee standing at £8,735 per year.

What do the party policies mean for universities, graduates and students?

That tuition fees do not appear to have harmed participation, and that the wage benefits of a degree remain strong, strengthens the argument for an increase in the fee cap (which the Conservative Party have so far refused to rule out), and could help create a market-driven system, with greater variation in tuition fee levels.

But such a system could be more expensive, given that it would mean fewer graduates repaying their loans in full. Thus, to make such a policy financially sustainable, the Conservatives would have to accompany their fee increase with punitive changes to the repayment system – potentially through raising the interest rate or reducing the threshold at which graduates repay their loans.

Labour have taken the opposite stance, promising to reduce the fee cap to £6,000 per year from 2016. The merits or otherwise of this policy depend on whose point of view you take.

Among graduates, the only beneficiaries of this policy would be high earners. A cut to £6,000 would only benefit those graduates who earn enough to repay their loans in full, or who manage to pay back annual fee debts somewhere between £6,000 and £9,000 – top earners. The remainder don't earn enough to repay their loans even at £6,000 so could never benefit from a fee cut.

Since fee loans are paid off after graduation, the fee cut will not help students either. Though Labour's pledge to increase grants by £400 will be of some help to the poorest students. While this is a fairly small increase, student support does matter for participation. Dearden et al find a £1,000 increase in maintenance grants increases participation by just under 4 percentage points.

What about prospective students? There is some evidence that many young people are still put off from going to university because of the cost, so Labour's policy could have a positive psychological effect and result in an increase in participation.

From the point of view of universities, however, the policy is not desirable. If Labour do compensate the £2.7 billion cost of the reform from tax rises, universities will be no worse off financially. But a larger part of university budgets would again become reliant on the whim of government. Moreover, the policy would end the hopes of creating a more competitive system for universities to increase quality and cost effectiveness. And yet another change in the funding system is a recipe for further uncertainty and instability in a system that has seen many changes over the past two decades.

This article is part of the CEP's series of briefings on the policy issues in the May 2015 General Election. See the longer version here. Or watch this video:

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