Understanding your market position ready for the new era

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1 The backdrop

The world has changed

- **Proposition 1: the world has changed**: 50 years ago higher education was not important in economic terms. Today it matters:
  - To promote core values (as always)
  - To pursue knowledge for its own sake (as always)
  - To promote economic growth in competitive economy
    - Technological advance a major driver
    - Higher education is vital both for national economic performance and for individual life chances
- Specific objectives: widening participation, quality, efficiency

What's ideological and what isn't?

- Balance between market and state: mainly technical, rooted in the economics of information
- Ideological: widening participation
- **Proposition 2: students matter**

2 The current strategy

Leg 1: paying for universities: deferred variable fees

Variable fees

- Promote quality
  - by bringing in more resources, and
  - by strengthening competition, creating incentives to use those resources efficiently
- Counter intuitively, variable fees are also fairer
  - Why should a student at Balls Pond Road Tech pay the same fee as at a world-class university?
  - Given the gradient in participation, arguing for higher fee subsidies is like arguing for higher champagne subsidies

Mistake to avoid: ‘big bang’ liberalisation

Does competition work?

- Yes when consumers are well informed
- Are consumers well informed?
  - Students are mostly a savvy, streetwise bunch
  - Much information is available and more can and should be made available
  - Good information is a central source of quality assurance:
    - On the student experience
    - On teaching
    - On employment outcomes

Leg 2: student support: free at the point of use

- Loans should
  - Have income-contingent repayments
  - Adequate, i.e. large enough to cover all fees and all living cost
  - Universal: all students should be entitled to the full loan
- Thus
  - Higher education is free at the point of use
  - Students are no longer poor
  - Students are not forced to rely on parental contributions, extensive paid work or expensive credit card debt
- Mistake to avoid: blanket interest subsidies

Loan repayments in the UK (2006 scheme)

	Bill	Tariq	Tim	Jane
Annual earnings	£15,000	£20,000	£30,000	£50,000
Income tax (monthly)	£161.19	£252.86	£436.19	£945.58
NI contributions (monthly)	£91.26	£137.10	£228.76	£274.93
Loan repayments (monthly)	£0.00	£37.50	£112.50	£262.50

- Low earners make low or no repayments
- Repayments automatically and instantly track changes in earnings, exactly like income tax and national insurance contributions
- Loan repayments are generally much smaller than income tax or national insurance contributions

Leg 3: active measures to promote access

- Widening participation
  - Raising attainment
  - Improving information/raising aspirations
  - Money measures

Mistake to avoid: underestimating the influence of attainment

What are the real determinants of participation?

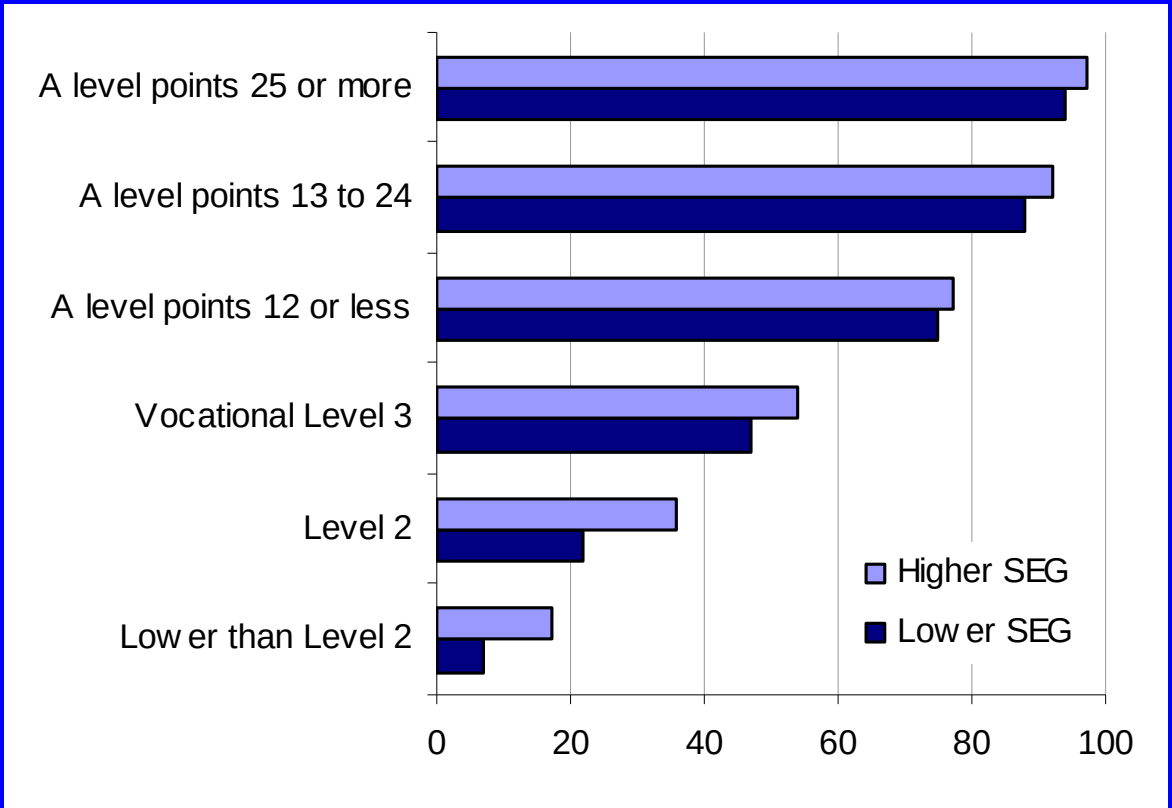
- According to ‘pub economics’ it is obvious that ‘free’ higher education widens participation
- Pub economics is wrong

If all else fails, look at the evidence

- Where are there the biggest social benefits?
  - Answer: at younger ages
- Where is the most public money spent?
  - Answer: at later ages
- Who gets the best GCSEs?
  - Answer: the children of professionals
- Who stays on after 16?
  - Answer: those with the best GCSE marks
- Who goes to university?
  - Answer: those with the best A level marks

Who goes to university? It's attainment, stupid

Source: Office for National Statistics (2004, Figure 2.15)



3 What can go wrong?

- Leg 1: Mistaken policies about the fees cap
  - Freezing the cap, or
  - Abolishing it
- Leg 2: Failure to grasp the nettle of the blanket interest subsidy on student loans
- Leg 3: Continued posturing about access rather than addressing the *real* problem – attainment in school

3.1 What should happen to the fees cap?

Why a fees cap?

- The fees cap should be
  - High enough
    - To bring in significant extra resources
    - To create genuine competition
  - Low enough
    - To maintain political sustainability by giving students, prospective students and their parents time to adjust
    - To give institutions time to put in place management suitable for a more competitive environment
- Should some sort of fees cap be permanent? Yes
    - To protect against exploitation of monopoly elements

At what level?

- A balancing act
  - Message to the access warriors: don't perpetuate a middle-class subsidy
  - Message to the market warriors: don't overshoot (USA)
- Essential that any increase in the fees cap is fully covered by an increased loan entitlement

3.2 What should happen to blanket interest subsidies

- The interest rate on student loans is equal to the inflation rate
- Thus students/graduates pay a zero real interest rate, lower than the rate at which the government borrows

What is wrong with a blanket interest subsidy?

A zero real interest rate

- Is enormously expensive, at least £1,200 million per year
- Impedes quality. Student support, being politically salient, crowds out the funding of universities
- Impedes access. Loans are expensive, therefore rationed and therefore too small
- Is deeply regressive, the main beneficiaries being successful professionals in mid career

What should be done?

- The blanket interest subsidy should be replaced by targeted interest subsidies
- The default interest rate should be related to the government's cost of borrowing
- Targeted interest subsidies should prevent real debt rising for
  - People with low earnings
  - People with caring responsibilities
- Targeted subsidies are administratively feasible (Hungary)

3.3 What policies *really* widen participation?

Before and during university

- Why does access fail? Substantially a 0-16 issue
  - Low attainment
  - Lack of information/aspirations
  - Lack of money
- Need policies to address all three
  - Early education measures
    - Early child development
    - Life cycle approach to education spending
  - Information/aspirations: an important role for universities:
    - Mentoring by students visiting schools
    - Visits by pupils to university, e.g. Saturday School, Summer School
  - Money measures include
    - Education Maintenance Allowances
    - University grants/bursaries

After university

- Income-contingent repayments
- Targeted interest subsidies
- Write off loans for selected groups
  - Public service workers
    - Teachers, nurses
    - Doctors
  - Carers, e.g. 10% pre-school age, 5% school age

4 Understanding your market position

The medium term

- **Proposition 3: not a free market but a regulated market**
  - Universities set fees, subject to a fees cap
  - Governments pay block grants; the balance between fees and block grants determines the extent of competition
  - Students apply to the institutions and courses of their choice
- A continuing broad role for government
  - To provide taxpayer support for higher education
  - To regulate the system
    - A fees cap
    - Ensuring that there is effective quality assurance (more below)
  - To set incentives, e.g. larger subsidies for certain subjects
  - To ensure that there is a good loan scheme
  - To promote policies that widen participation

The shorter term: many factors cut both ways

- Some parts of the economy have a counter-cyclical aspect
- Universities
  - Higher education becomes relatively more attractive to build skills at a time when job prospects are not good, hence the opportunity cost of study is lower
  - A falling exchange rate helps universities with students from other countries
- The labour market
  - Parental jobs may suffer
  - Student jobs: employers may trade down, with rising number of jobs for students, directly or via agency jobs
- Marketing
  - Clear links with quality assurance
  - Not just prices – students choose on great variety of criteria
  - The fees cap contains competitive pressures

Conclusion

- At risk of sounding like Pollyanna, my main message is: don’t panic
- Upheaval creates many new opportunities (worms in ploughed field)
- Short-run crisis, long-run brain
- A regulated market, not a free market

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