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Understanding the Further Education  
Market in England: Executive  
Summary

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RESEARCH

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# Executive Summary

Further Education (FE) in England refers to any study taken after the age of 16 that is not part of higher education (that is, not taken as part of an undergraduate or post-graduate degree)<sup>1</sup>. It is delivered by a range of public, private and voluntary sector providers and, in general, equips a learner for further learning, including Higher Education, or for employment. It also plays an important role in reaching out to disadvantaged groups to encourage their participation in learning when they otherwise might not.

To inform decisions about how best to fund and regulate the FE market so that it can deliver effectively for learners and employers<sup>2</sup> and contribute to a skilled and productive workforce, this report has four key objectives. They are to:

1. **Describe the FE market<sup>3</sup> and its sub “markets”**: the economic structure, policy landscape and key players in the market;
2. **Investigate the extent to which we observe features in the FE market and its sub “markets” that are common to well-functioning markets** and to identify where such features would not be appropriate given the wider objectives of FE;
3. **Identify the barriers that prevent the FE “markets” from functioning effectively**; and therefore,
4. Stimulate discussion of **priorities for policy intervention** to improve effectiveness.

In this report, we focus on the publicly funded components of the FE market and not the wide range of education and training that is privately funded by employers for their staff. We also exclude other study that FE providers may offer within the school and Higher Education systems e.g. vocational provision for 14-16 year olds.

## Our approach

To carry out the analysis we have drawn on three substantive forms of evidence. Firstly, we have reviewed published literature including academic publications, research reports, statistical publications, guidance documents, government policy documents, provider annual reports, financial statements and legislation. Secondly, we have carried out detailed quantitative analysis using the Individualised Learner Record (ILR) for 2013/14; the National Course Directory; and the Provider Information Management System (PIMS).

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<sup>1</sup> This is the definition used by government. See <https://www.gov.uk/further-education-courses/overview>.

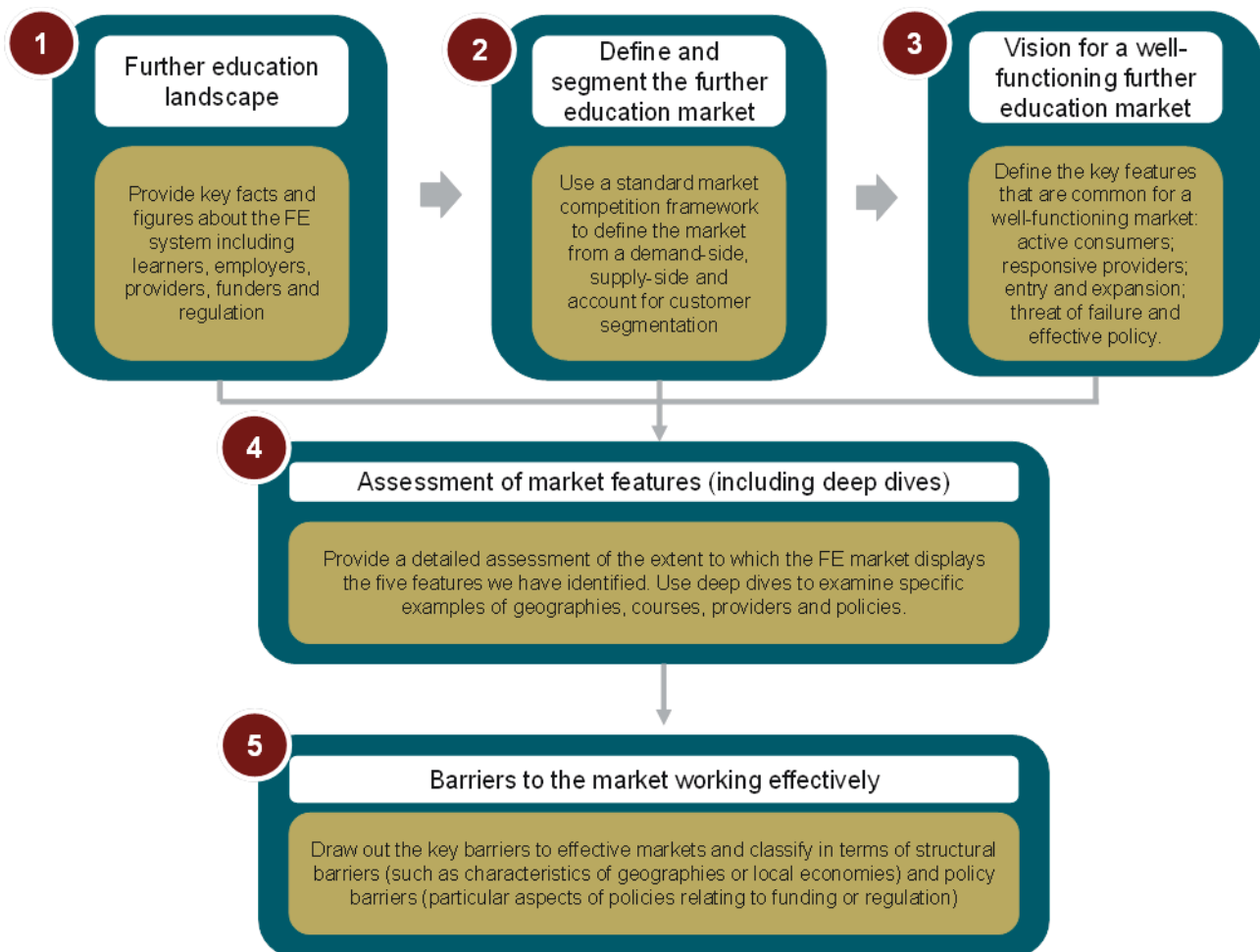
<sup>2</sup> Although the term “employers” is used throughout this report, this also includes self-employed individuals as they make decisions about their own training.

<sup>3</sup> For the purposes of this study we are focusing on publicly funded and regulated FE (including direct funding and via loans) in England only. We are not including the wider work that some FE providers undertake, such as provision for those still in school (14-16), provision of programmes of prescribed higher education or overseas skills activities.

Thirdly, we have developed a deep understanding of FE through a series of around sixty semi-structured interviews with stakeholders across the market<sup>4</sup>.

Using this evidence, we have focused on understanding five areas of analysis as shown in Figure 1.

**Figure 1. The five steps in our approach to this study**



Our analysis is presented for each of these five areas in turn.

## The FE landscape

The FE market is highly complex. It engages with millions of learners (around 4 million publicly funded learners in 2013/14) from a wide range of backgrounds and reaches out to many more not yet participating in FE. Most FE learners are over 19 years of age (75%) with just 25% under 19. Learners participate in learning with one of around 1,150 publicly funded<sup>5</sup> FE providers across the country.

<sup>4</sup> See Annex 1 for a full list.

<sup>5</sup> Here we refer to those holding direct contracts with the Skills Funding Agency or Education Funding Agency.

The total public budget for FE in 2013/14 was over £10 billion. The Skills Funding Agency (SFA) provides £3.8 billion of funding for further education divided into the Adult Skills Budget worth £2.1 billion<sup>6</sup> and the Apprenticeship budget worth £1.4 billion in 2013/14<sup>7</sup>. The remainder of the SFA budget includes student/ learner support. The Education Funding Agency (EFA)<sup>8</sup> funding was £6.2 billion. A further £159 million was provided by the European Social Fund (ESF).

## Learners

In 2013/14 there were around **4 million learners** from a wide range of backgrounds in the further education market. The provider-base is **diverse** but learners were participating at General FE and Tertiary Colleges, private, independent and voluntary providers (publicly funded), School Sixth Forms, employers, Sixth Form Colleges, special colleges (including Agriculture and Horticulture Colleges; Art, Design and Performing Arts Colleges; and, Specialist Designated Colleges) and other publicly funded providers (such as Local Authorities and Higher Education institutions).

Alongside participating at one of the FE learning institutions above, workplace-based learning is also a notable feature of the market. Of all learners, some 851,500 are currently participating in an apprenticeship with the majority of apprentices being adults aged 19 years or above.

Learner's decision-making about what to study and where to study is complex. A wide range of factors influence decisions including informal advice from families, guardians or peers; the reputation of the provider and the type of **setting** (whether to learn in a multi-disciplinary setting, with a small independent provider or in a community-based setting).

Learners' choices about FE, at present, tend to be **very localised**. Most learners (70%) travel less than 10km from their home to the site of their provider, with 50% travelling less than 6km. Distances travelled vary by subject area and course. Time and cost of travel are key constraints. The distance travelled by learners appears to be generally lower for basic subject areas like Preparation for Life than for more specialised areas like Health and Social Care and Engineering and Manufacturing. Learners tend to travel shorter distances to their provider around big cities - such as London, Manchester and Birmingham – and longer distances in more rural areas like Norfolk and Cornwall.

## FE Provision

Education and training within the publicly funded FE market is, at present, largely structured around **qualifications** – there are over 15,000 qualifications on the Ofqual Register of Regulated Qualifications, both academic and vocational, a wide range of levels and a broad range of sector specialisms. Qualifications are offered in a variety of settings and learning modes. **“Core”** areas of provision offered by most providers are preparation

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<sup>6</sup> This includes Adult Community Learning and funding for the Offending Learning and Skills Service (OLASS)

<sup>7</sup> Alongside funding for apprenticeships for learners aged 19+, the SFA allocates 16-18 apprenticeship funding on behalf of the Department for Education.

<sup>8</sup> This includes funding for schools and FE providers and student support funding.

for life and work courses<sup>9</sup> (98% of providers); business, administration and law courses (87%); and health, public services and social care courses (72%). Less commonly offered subjects are social sciences, history, philosophy and theology and agriculture, horticulture and animal care. The largest expansions in provision since 2011/12 have been in retail and commercial enterprise programmes; education courses; and business, administration and law courses. The majority of learners (over 40%) are studying for a **level 2** qualification.

There are 1,150 FE providers in direct receipt of public funding, ranging from charitable organisations and non-profits to private companies and FE Colleges. The total number of providers offering publicly funded FE provision is likely to be much higher as **subcontracting** is a significant feature of the market, accounting for £780 million of contract commitments in 2014. Subcontracts are typically long standing (more than 5 years), focused on 16-18 apprenticeship and 19+ apprenticeship provision and particularly present in the construction, and health and care sectors. Lead providers typically retain between 5% and 30% of subcontractors' funding as management fees.

There has been **minimal entry** into the government funded FE sector over the last 3 years (except for entry of School 6th forms<sup>10</sup> of which we understand approximately 260 have entered over the four years from 2011/12 to 2014/15) but there has been **extensive merger and consolidation** activity and also a notable number of **exits** of private providers. Providers have, however, been **flexing their offers** considerably over this period with more than 50% expanding into new subject areas and 35% withdrawing from subject areas.

## The FE workforce

It is estimated that there are over 326,00<sup>11</sup> staff working across the FE sector<sup>12</sup> with approximately 250,000 staff in colleges<sup>13</sup>, 51,000 staff in Work-based learning training<sup>14</sup> providers and 25,000 staff working in Local Authority providers of Adult and Community Learning. The majority of the workforce is aged 35 years or over and part-time working is extremely common. There is also some dependence on volunteer teachers within the sector.

FE providers report recruitment difficulties most frequently in functional skills, mathematics/numeracy and English/literacy. However, there is also a concern within the sector that high quality teaching and training relies on a clear line of sight to work<sup>15</sup>. This means that teachers and learners need to be continually exposed to new forms of knowledge and practice to perform at their best. It is reported that identifying either skilled

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<sup>9</sup> Including basic English and Maths.

<sup>10</sup> Including new free schools, University Technical Colleges and studio schools.

<sup>11</sup> This figure excludes staff working in School Sixth Forms.

<sup>12</sup> Workforce data across the Further Education sector – 2013-14, Education Training Foundation

<sup>13</sup> Including General FE Colleges, Sixth Form Colleges, Agricultural and Horticultural Colleges, Arts Colleges and Specialist Designated Colleges.

<sup>14</sup> Including independent training providers, third sector/charity training providers, Group Training Organisations and employers providing training.

<sup>15</sup> "It's about work... Excellent adult vocational teaching and learning", Commission on Adult Vocational Teaching and Learning, 2013

professionals or teachers able to offer training of this nature in some localities and occupations can be a particular recruitment difficulty.

## FE Funding and regulation

As noted above, the total public budget for the FE market in 2013/14 was over £10 billion. The SFA provides £3.8 billion of funding for further education divided into the Adult Skills Budget worth £2.1 billion<sup>16</sup> and the Apprenticeship budget worth £1.4 billion in 2013/14<sup>17</sup>. The remainder of the budget includes student/ learner support. Some £6.2 billion is provided by the EFA<sup>18</sup>. A further £159 million was provided by the European Social Fund (ESF). Around 60% of total funding goes to Further Education Colleges and Tertiary Colleges.

The EFA funds FE for young people aged between 16 and 19. Providers receive a funding allocation, based on the number of students, reflecting the number of students enrolled last year and an adjusted national funding rate per student.

Adult funding is administered by the SFA. The adult funding model applies to all learners aged 19+ and is currently based on qualifications with each qualification assigned a funding rate according to the size of the provision (credits or guided learning hours) and a programme cost weighting. For apprentices aged 19 and older, the SFA covers up to 50% of the funding rate, with the employer expected to make a contribution. Also, with effect from 1 August 2013, learners aged 24 and older wanting to study qualifications at Levels 3 and 4 are no longer funded by SFA. Those learners on eligible courses at these levels can apply for a **24+ advanced learning loan** to pay for their studies.

FE providers in receipt of government funding are subject to a range of **regulations**. They must be on the SFA's Register of Training Organisations and subject to appropriate due diligence. They are subject to regular quality inspections by **Ofsted** and financial health checks and if they fail to pass either of these, or fail to meet minimum standards, further action is triggered. For example, private providers could be issued with a notice to terminate their contracts with the SFA, or the FE Commissioner may become involved for Colleges or other particular providers under the remit of the Commissioner.

## Defining the FE 'market'

The FE market is complex and seeks to meet the needs of a wide range of groups within the context of regulation to ensure quality, and substantial public funding to ensure wide accessibility to learning.

Although we refer to FE as a 'market' throughout the rest of this report, the level of government funding and the role of government and public agencies in the way FE is delivered mean it is not a typical 'market'. In a typical market, 'consumers' and 'providers'

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<sup>16</sup> This includes Adult Community Learning and funding for the Offending Learning and Skills Service (OLASS)

<sup>17</sup> Alongside funding for apprenticeships for learners aged 19+, the SFA allocates 16-18 apprenticeship funding on behalf of the Department for Education

<sup>18</sup> Covering funding for schools and FE providers.



interact with the resulting outcome presumed to be the best for society. This is not the case in FE for several reasons:

- Learning delivers wider benefits to society that go well beyond the benefits to those participating, and their subsequent employers.
- Learners do not ‘consume’ learning in a conventional way but rather participate in learning to enhance their skills and capabilities – some choose to do so, yet for others, participation is a government requirement (for example, JobCentre Plus referrals). Many learners do not pay to learn (government pays for them) yet some do pay towards their learning.
- Employers do not consume learning either – they reap the rewards from having a more highly skilled workforce, and reflect the value of those skills in salaries. Both learners and employers can however be seen to benefit from learning and one or both may contribute to the cost of its provision.
- Many providers do not compete on the price of their services as is common in many markets, but rather on the quality and relevance of their provision. However, as this report will later show, some may not ‘compete’ with others at all; and in some parts of the market learners do not choose providers but providers (e.g. selective 6th forms) choose learners.

Despite not being a typical ‘market’, this study investigates the effectiveness of the FE market through an economic lens. Although this is not straightforward, there are elements of the FE market that do demonstrate features typical to any market and for these, our economic framework is appropriate. We therefore apply our framework where it is appropriate to do so, and have adapted it where it is not to recognise the uniqueness and the various market failures and non-market objectives of the FE market.

We have identified 7 market groupings within the FE market using a commonly applied market definition framework that considers the substitutes available to consumers, the ease with which suppliers can switch between different products and geographies as well as the different choice conditions faced by some customer groups. The market groupings (divided into local, regional and national markets) are:

## Local markets

1. **Local “core” mixed environment training**<sup>19</sup>, covering levels 0 to 3 and leisure courses. Within this market there are distinct customer segments for 16-18 year olds (who have a wider range of choice of providers than 19+ year olds) as well as for those learners routed via JobCentre Plus who may have little choice of provider.
2. **Local, “basic” community-based training**, covering levels 0 and 1 as well as adult community learning courses that do not lead to a qualification.

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<sup>19</sup> A provider offering courses across a range of sectors and subjects, for example a FE College.

## Regional markets

3. **Capital intensive training, offered from a FE provider's site** (rather than in the workplace), covering all qualification levels.
4. **Regional "advanced" sector-focused training**, covering level 4+ but only on courses that are not capital intensive<sup>20</sup>.

## National markets

5. **Sector focused training in the workplace**, covering all levels, with a distinct customer segment for large employers
6. **Specialist (often residential) provision**
7. **Prison-based learning**

These definitions were reached following detailed consideration of the learners' decision whether to participate in FE and if so, how, as well as the providers' decision about what to provide. The division of the FE market into these groups is reflective of the different structural characteristics and policy framework at play in these different parts of the FE system.

## A vision for a well-functioning FE market

Ultimately, the question that government would like to be able to answer is whether the FE market is delivering the most appropriate outcomes for learners, employers and the economy more generally – could the private and social returns be higher? This is clearly an extremely challenging question as there is no obvious counterfactual to which the FE market today can be readily compared – no one knows what outcomes would look like under a different market system.

The FE market is subject to government intervention in a range of forms, many of which have been implemented to overcome market failures that would mean the FE market, left to its own devices, would not be expected to fully deliver the outcomes desired by society. Despite the recognition that government intervention is needed, there is also a view that the market mechanism plays a key role within FE.

The starting point for this work was therefore to determine whether the sub-markets within the FE sector were working as effectively as they could. Implicitly this is a two stage question where stage 1 asks whether and where markets have the potential to be effective in FE and stage 2, where they could be effective, are they working as well as they could?

To frame our work, we posed the question: "what features would need to be observed across the FE market to ensure that it could, and is, functioning well as a set of markets?"

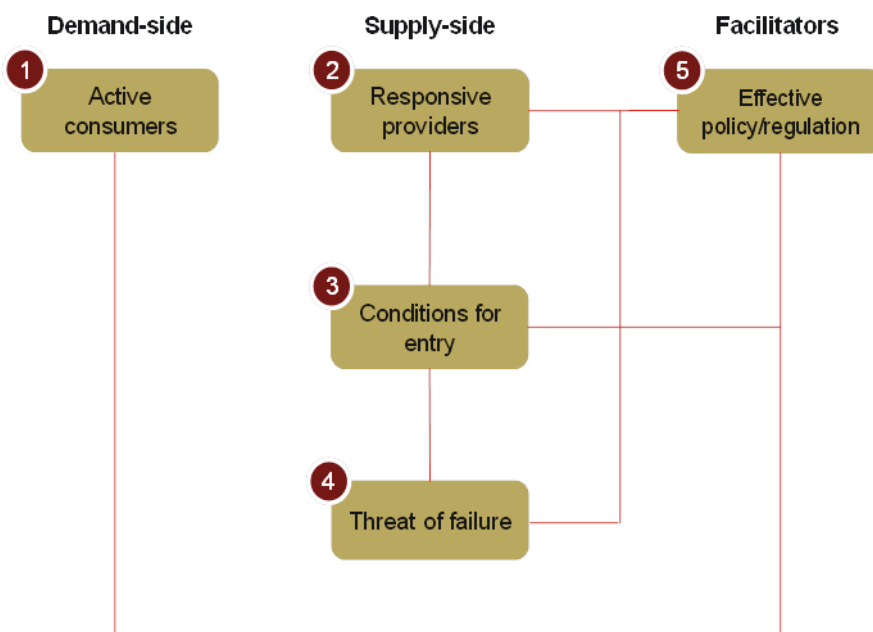
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<sup>20</sup> Both groupings 3 and 4 address the technical and professional training that are currently government priorities. Here we split them according to capital intensive provision at all levels; and advanced (level 4+) training.

This “vision” of a well-functioning FE market (shown in Figure 2) is the benchmark against which we compared the FE markets we observed in practice. The comparison enabled us to make an assessment of what is working well and what is not in each of the seven sub-market groupings we have identified.

Akin to other market studies, we considered the consumer (demand) side and the provider (supply) side of the markets. We asked whether or not consumers and providers were incentivised and able to provide competitive pressure in this market. In addition we considered the role that policy and regulation play in this market. We considered whether policy and regulation are successfully targeting those areas where the demand and supply side do not provide sufficient incentives for driving up quality, efficiency and innovation i.e. where the market fails.

**Figure 2. Features of a well-functioning FE market**






- **Active consumers** – covering the features we would expect to see in a market that facilitate consumers being active. These include availability of choice; information about those choices and accessibility of that information; and confidence and ability to make an informed choice. Evidence of consumers making active choices is also considered.
- **Responsive providers** – covering the extent to which providers are incentivised and able to respond to market pressures unconstrained by structural market conditions, governance arrangements or policy and regulation. Evidence of providers being responsive is also considered.
- **Conditions for entry** – covering the extent to which the market is open to entry by new providers or whether there are significant barriers which could be structural in nature or policy driven.
- **Threat of failure** – covering the extent to which poor performers can straightforwardly exit the market and whether policy allows a clear and credible threat of provider failure.
- **Effective policy/regulation** - covering the extent to which policy and regulation ensure that competitive pressures are enabled (and not distorted or reduced), and supplemented where appropriate (e.g. where there are structural market failures) and that there are appropriate safeguards for consumers.

## Our assessment of the market against that vision

### Where the market is working well

Our analysis identified various aspects of the FE system and its sub-markets that display characteristics associated with well-functioning markets. Examples include:

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**Provider responsiveness:** our analysis suggests that providers are generally very responsive to learners, competitors and policy. Many actively monitor the market to understand learner and employer needs and competitors' offers and adapt their FE offer accordingly.
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**Learner choice:** Even though the market considered by learners is typically very local, learners generally do appear to exercise some local choice. Typically only 20-30% of learners use their nearest provider.
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**Ability to expand or change the FE offer:** evidence suggests that most providers are not unduly constrained from adapting their FE offer. In recent years, some have expanded into new areas of provision in response to local demand and policy (such as apprenticeships), and others have actively chosen to withdraw from some forms of provision (such as A-levels) so that they can concentrate on providing other forms of FE.

There are, however, a number of barriers that prevent the market from working well and cut across several of the features we have identified.

### Cross-cutting barriers preventing the market from working well

Our analysis suggests that there are some markets in which learners have a very limited choice of alternatives, and providers have a limited set of likely competitors. Our analysis shows that:

- learners typically have more choice for general courses than they do for more specialised courses;
- learners in some areas tend to have few college alternatives available within their catchment area<sup>21</sup>; and
- some courses such as specialised engineering courses, exhibit pockets of 'not spots' i.e. areas where there are no providers.

The lack of alternatives can be entirely the appropriate market outcome where structural features of the market including the nature of the investment involved, and the number of potential learners, mean that only a single or small number of providers can be supported viably by the market. For example, in some areas of the country the learner base may only be large enough to support one provider of a viable size (because of economies of scale in


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<sup>21</sup> Defined as a 10km radius, reflecting the fact that 70% of learners are drawn from that radius. Traditionally, a cut of closer to 80-90% would be used to define geographical catchments but the data used for this study suggests that, in this context, 70% is an appropriate cut off.

provision). For markets displaying these structural characteristics, competition may not provide sufficient incentives for efficiency, quality and innovation. These markets display “structural barriers” to competition.

However, in markets where the limited set of competitors is not the result of structural features, policy changes may be able to enhance the workings of the competitive market to improve outcomes. For these markets there are “policy barriers” to competition. These two sets of barriers are set out in Table 1 below. Before turning to the table, it is worth noting that in many markets both types of barriers are likely to be at play, so detailed consideration at a market by market level is required to identify those markets where policy changes should be sufficient to enhance the market mechanism and those where other supplementary incentive mechanisms may be required.

**Table 1. Availability of alternative competing providers**

	Structural barriers	Policy barriers
<b>Barriers to entry</b> 	<ul style="list-style-type: none"> <li>• Natural monopolies – low market demand coupled with a minimum efficient scale for provision can mean that few alternative providers can be sustained in some markets (entry will be limited). Likely to be an <b>issue for areas with a low or dispersed learner base</b>.</li> <li>• Large, predominantly sunk investment costs generate a barrier to entry in markets where they are fixed and difficult to recover post-entry. This is a particular issue for <b>capital intensive parts of the FE market with very specific assets</b>. It may also be important for <b>college-based provision where reputation and history</b> (requiring significant investment to overcome) can play a key role in learner recruitment.</li> <li>• <b>Pension regulations</b> for Colleges as defined in the 1992 Further and Higher Education Act can also represent significant liabilities for Colleges, acting as both a barrier to entry and exit.</li> <li>• <b>Cost of switching Awarding Body</b> (or working with multiple Awarding Bodies) can limit entry and hence the number of alternative providers in some parts of the market.</li> <li>• <b>Staff shortages</b> in some areas (particularly those where providers must compete against other teaching professions and the trade/industry) can limit entry and hence the number of alternative providers in some parts of the market.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Lack of direct SFA contracts</b> - access to direct contracts is limited because there are very few, if any, new direct contracts and current direct contracts roll on as long as providers meet minimum standards. Range of providers may be constrained by this in some areas of the market as subcontracting is the only route of market.</li> <li>• <b>Historic reluctance to close a college</b> creates a barrier to entry as new entrants would not have the confidence that they would be able to displace the incumbent even if they are able to offer a superior training offer.</li> </ul>

	Structural barriers	Policy barriers
	<ul style="list-style-type: none"> <li>Local economy – the availability of apprenticeships as well as the demand for other types of vocational training is very dependent on the composition of the local economy. Range of provision may be limited in areas where <b>local demand and opportunities are limited</b>.</li> </ul>	
<b>Level playing field</b>	 <ul style="list-style-type: none"> <li>Narrow focus of some providers: the risk of not being able to adequately respond to or manage policy changes can be greater for smaller providers. For example, if policy priorities shift funding away from their core areas of business. These providers are <b>naturally more exposed to risk</b>.</li> </ul>	<ul style="list-style-type: none"> <li>Colleges receive much greater <b>support</b> than independent providers <b>to avoid closure</b>, limiting the scope of independent providers to enter and expand in some markets where colleges have a heavy presence.</li> <li>Ability of those with direct contracts to use <b>subcontracting as a means of propping themselves up</b> in the event of poor performance. Again, limiting the scope of other providers to enter or expand.</li> <li><b>Differential VAT regime</b> – Schools 6th Forms benefit from preferential VAT regime but Sixth Form Colleges and General FE Colleges do not affecting their ability to compete effectively in some parts of the FE market.</li> </ul>
<b>Barriers to exit</b>	 <ul style="list-style-type: none"> <li><b>Pension regulations</b> for colleges can act as both a barrier to entry and exit.</li> <li>There are no <b>formal administration</b> and insolvency procedures for Colleges – a further potential barrier to exit</li> </ul>	<ul style="list-style-type: none"> <li><b>Lack of formal requirement to secure continuity of provision</b> for learners upon exit can increase reluctance to allow exit of large providers – this is a barrier to exit.</li> <li><b>College assets</b> must only be used for educational purposes, limiting the ability for complete exit of some provision.</li> </ul>



As well as cross-cutting barriers that restrict the range of alternative providers able to operate in the FE system and its specific sub-markets, there are a range of other barriers that may limit the effectiveness of the market mechanism as a means of driving up performance in FE. We consider the barriers to active consumers and responsive providers in turn. We then turn to the policy and regulatory challenges inherent in the system.

## Further barriers affecting active consumers

A well-functioning further education market requires its consumers<sup>22</sup> (learners and employers) to be **active**. That is, consumers – or perhaps ‘beneficiaries’ – of further education should be able to make informed decisions about learning options that meet their own best interests, and also send a signal to the market about what those interests (or needs) are. In turn, providers have an incentive to meet those needs.

For the purposes of this report, we have defined consumers as “active” in the context of FE if they have an available choice, an awareness of that choice, access to information to appropriately guide that choice and confidence and ability to make a good choice. Table 2 summarises the barriers to consumers being “active” in this market that we have identified.

**Table 2. Barriers to active consumers**

	Structural barriers	Policy barriers
<b>Awareness of choice/ access to information</b> 	<ul style="list-style-type: none"> <li>Limited direct communication between employers and learners means learners may not be aware of all their options or potential career paths.</li> <li>Too much information available on the internet can confuse learners about who to trust.</li> <li>Reliance on informal channels of advice (families, guardians, peers) could affect the perceived available choice.</li> <li>Lack of impartial advice from schools (they have the incentive to retain learners) could restrict learners’ awareness of choice</li> <li>Lack of information to certain groups, such as employees in low paid work, limits awareness of choice e.g. National Careers Service focuses on disadvantaged groups.</li> </ul>	<ul style="list-style-type: none"> <li>Poorly targeted information – available information is not well targeted for different learners (e.g. some would like employment rates, salaries).</li> <li>Lack of awareness of some employers of options relating to apprenticeships.</li> </ul>
<b>Confidence and ability to make decisions</b> 	<ul style="list-style-type: none"> <li>Inability to judge quality or relevance of course can limit learners’ ability to make informed decisions.</li> <li>Individuals not actively seeking to participate: some disadvantaged groups are below the radar of the FE market.</li> </ul>	<ul style="list-style-type: none"> <li>Lack of guidance and support to learners when making choices. Only 2/3rd of learners satisfied with the information they were given when choosing their course.</li> <li>Others decide on learners’ behalf – e.g. JobCentre Plus mentors; some employers choose the provider for their employees.</li> </ul>

<sup>22</sup> Or at least a meaningful subset of consumers.

## Further barriers affecting responsive providers

For the FE market to function well in terms of meeting the interests and needs of learners, employers and the government, providers need to be **responsive**. They need to be incentivised to improve the quality and suitability of their offer to learners and employers as well as the efficiency of their offer to ensure they remain profitable at the prevailing funding rates. The incentives faced by providers are likely to vary according to the degree of competition they face from alternative providers and the extent to which the funding arrangements for their provision are a clear threat to their profitability.

For the purposes of this report, we have considered whether providers are constrained in some way from responding to those incentives. As with any diverse market, there are elements of good practice in terms of responsiveness such as providers that undertake studies of demand, engage actively with employers and sector bodies and keep active track of what their competitors are doing. But, there are also instances where providers appear not to be responsive, either because they lack the incentive to or because they face barriers in so doing.

Although there is evidence to suggest that many providers are responsive to learners, employers, competitors and policy, there are also some clear barriers that have limited responsiveness for some providers in some markets.

- **Limited scope of operation** – providers offering a limited range of courses are a common feature in the market but these providers may find it hard to respond to changes in learner and employer demands, competition or policy because of their limited scope.
- **Cost of switching awarding bodies** - providers must adhere to the awarding body requirements to be eligible for funding. Although awarding bodies allow some flexibility, this may be insufficient and there appear to be high costs associated with changing awarding bodies, further hindering their ability to respond quickly. Adding to that, few providers of FE are awarding bodies themselves, despite several providers commenting that they would like to be.
- **Short lead times of funding allocations and only a single year allocation** - these short lead times can hinder longer term planning and space for innovation and can make it difficult to invest in line demand.
- **Funding limits for independent providers** – independent providers face a cap on the level of provision they are able to deliver. This can constrain them amending their provision to meet higher than expected levels of learner demand.
- **Policy instability & uncertainty** - reduces the ability of providers to plan ahead and release resources for innovation. Specialised providers are arguably at greater risk of changes in policy priorities and funding because they have centred their business model on a certain type of provision.
- **Staff shortages** - there are staff shortages for many subjects for both teaching and assessment (e.g. maths) as FE providers compete with schools, Higher Education and with their associated occupations for skilled staff. Further education providers





find it hard to attract skilled teachers away from other organisations that are able to pay more, including their trade or industry<sup>23</sup>.


- **Local employment markets** - the employment and economic composition of a provider’s catchment area can make a significant difference to their ability to respond to policy incentives. This is particularly true in the case of apprenticeships.
- **Inadequate provider governance** - weak governance and a lack of expertise and management skills are likely to be among the causes of provider difficulties in terms of responsiveness to market conditions. In some cases FE College leaders were not trained in how to manage such large ‘businesses’ as FE Colleges. In a minority of cases there are also problems around the length of board tenures.

Table 3 summarises these barriers.

**Table 3. Barriers to responsive providers**

	Structural barriers	Policy barriers
<b>Ability to respond to learners and employers</b> 	<ul style="list-style-type: none"> <li>• Size of provider – smaller providers could find it more difficult to make significant changes to their FE offer</li> <li>• Staff shortages - can hinder the ability to provide those courses despite demand</li> <li>• High costs of changing awarding bodies – providers need to invest significant resources to re-train staff, purchase new teaching equipment</li> </ul>	<ul style="list-style-type: none"> <li>• Difficulty in gaining awarding body status can in some cases hinder providers’ ability to respond to employer needs.</li> <li>• One year funding allocations – these make it difficult to plan ahead and can deter investment to better respond to learner or employer demand.</li> <li>• SFA contracts for independent providers are capped and therefore it is difficult for providers to respond to changes in demand - they are not funded for any provision in excess of the cap.</li> </ul>
<b>Ability to respond to competitors</b> 	<ul style="list-style-type: none"> <li>• Natural monopolies and a minimum efficient scale can put some providers at a natural cost advantage</li> <li>• Large, predominantly sunk investment costs could hinder the responsiveness of providers to enter new segments of the market. This is particularly an issue for capital intensive parts of the market with very specific assets or where reputation and history can play a key role in learner recruitment.</li> </ul>	<ul style="list-style-type: none"> <li>• Funding allocations based on previous year activity - where providers spot a market opportunity, in some cases it may not be straightforward to respond because funding will only change with a lag.</li> <li>• Multiple funding bodies - it may be difficult to change from focusing on one group of learners to another because of a required shift in funding streams e.g. EFA fund 16-19 year olds but SFA funds 19+</li> </ul>

<sup>23</sup> The Teach Too initiative seeks to address this

Structural barriers	Policy barriers
<p><b>Ability to respond to policy</b></p>  <ul style="list-style-type: none"> <li>Local employment markets – the composition of local employers may limit provider’s ability to respond to policy incentives, such as a shift to apprenticeships or to deliver 24+ Advanced Learner Loans.</li> <li>Underutilised or stranded assets - it can be difficult for providers to respond to policy incentives to shift to, for example, apprenticeships, if it leaves under-utilised or stranded assets from previous capital investments.</li> </ul>	<ul style="list-style-type: none"> <li>Apprenticeships are only available as full time jobs (30 hours or more) which may limit attractiveness for some learners, making it hard for providers to recruit them.</li> </ul>

## Policy and regulation challenges

In the context of facilitating a dynamic FE market, policy and regulation have a specific role to ensure three main things:

- that competitive pressures are enabled (and not distorted or reduced), where they are appropriate;
- that competitive pressures are supplemented with policy and regulation where there are structural market failures; and
- that appropriate safeguards for consumers are available in the event of provider failure or for vulnerable groups.




In the context of enabling competitive pressures, we find there is a role for policy to enable effective consumer decision making, ensure a level playing field and stable policy environment for providers and ensure that providers have sufficient flexibility and incentives to respond to consumer needs.

There are a number of areas within the FE market where there appear to be structural or natural market failures that mean that the competitive process is likely to be impeded. There is a role for policy in recognising and regulating any true natural monopolies (created by a combination of economies of scale in provision coupled with small catchments). There is also a role for policy to ensure that there is a coordination of provision across larger geographical areas where individual providers are incentivised to focus on local demand.

In the context of enabling competitive pressures, policy plays an important role in ensuring that the market works effectively but also recognising where competitive markets are not appropriate and providing alternative incentives for efficiency and quality. It also acts as a safeguard to learners.

Our analysis of these policy and regulatory challenges for FE is summarised in Table 4.

**Table 4. Policy and regulatory challenges**

Challenges for policy and regulation	
<b>Ability to enable competitive pressures</b>	 <ul style="list-style-type: none"> <li>• Lack of requirement for schools to provide impartial advice and guidance on the full range of options open to learners</li> <li>• Lack of targeting of public information sources towards the needs of different learner groups – lots of information available (e.g. FE Choices) but could be improved</li> <li>• Lack of rewards for activities to reach out to disadvantaged groups – funding system and quality assessments do not reward out-reach work with learners who may have lower retention rates</li> <li>• Single year funding allocations and little advanced notice of the next year's funding hinder longer-term planning and innovation</li> <li>• Funding system hinders new entry and competition in the market as direct contracts roll-on (as long as minimum standards are met)</li> <li>• Difficulty for FE providers to become awarding bodies could hinder innovation and ability for providers to meet employers' needs</li> </ul>
<b>Supplementing competitive pressures</b>	 <ul style="list-style-type: none"> <li>• Lack of regulatory framework to address any natural monopolies (economies of scale in provision coupled with low demand)</li> <li>• Lack of recognition in funding for the role of minimum efficient scale</li> <li>• Absence of systematic promotion of coordination of provision where minimum efficient scale means multiple providers would not be efficient, and without co-ordination, may lead to gaps</li> </ul>
<b>Safeguarding consumers</b>	 <ul style="list-style-type: none"> <li>• Lack of transparency around mechanisms to ensure quality of sub-contractors and workplace based training</li> <li>• Lack of widespread appropriate security of provision for learners in the event of exit of providers (SFA may not be appropriately involved, learners may discontinue their learning, administrative delays may occur) – many learners could be left stranded. SFA is only involved in finding alternative providers where direct contractors fail.</li> <li>• Lack of transparency and knowledge about interdependencies in the market caused by sub-contracting – this could lead to the impacts of a failure cascading widely to others in the market</li> </ul>

## Concluding remarks

The in-depth analysis undertaken for this study has found that in many areas of the FE market, we observe characteristics that are consistent with a well-functioning market. A key objective for policy is to therefore facilitate the continuation of what is working well and to identify those areas where there is a need for policy intervention. Some of the key policy implications are:

**Recognising the limitations of competition in the FE market:** we have shown that in some cases, there is limited choice for learners and there are few competing providers. This could reduce the incentive for provision to be innovative and efficient. However, in some cases competition would not be likely to lead to the best outcomes for learners

and employers because the market dynamics make competition (involving several providers) unviable. In such cases, alternative mechanisms for incentivising efficiency, quality and innovation are likely to be worthwhile.

**Addressing barriers to active consumers:** Our work suggests that learner decision-making is extremely complex and localised and choices may not always lead to the best further education or labour market outcomes for learners. The decision as to whether to participate in FE at all poses a particular problem for some key groups. Key issues include ensuring young people at school have access to impartial advice; engaging groups who might not otherwise participate in FE (often considered 'hard to reach'); and strengthening the links between potential learners and employers.

**Addressing barriers to responsive providers:** our analysis suggests variability in the extent to which providers are responsive to learners, employers, other providers with whom they compete and government (often a primary source of funding). This is often expected within a market as some providers will be subject to more pressures than others and some will be better able to respond, with poorer providers entering financial difficulties. The route to exit of poor providers must be clear but must also ensure that learners are not stranded without provision. The intervention process for all providers must be transparent, based on the same principles and create the incentive to deliver high quality FE efficiently. In addition, quality assessments must be appropriate and timely; and funding should not unduly inhibit flexibility to local market conditions or hinder changes to provision where there is local, regional or national demand.

**Addressing wider policy and regulatory challenges:** policy has a significant impact on the way the market operates, whether through funding, quality assessments or procedures for contracting. Sub-contracting offers clear value to providers and learners but aspects of it are not currently well understood, such as the interdependencies this creates across the FE market. Issues identified in this study include a lack of appropriately targeted impartial information for different learner groups; impacts of the funding market on the responsiveness of providers (such as short lead times for funding allocations) and the impacts of local structural barriers on the ability of providers and employers to respond to national policy signals.



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