

Response to the CMA Early Years Education and Childcare Market Study

Statement of Scope consultation

Litus Advisory Ltd

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Who I am

Litus Advisory advises early years operators and their investors on margin, cost per funded hour and commercial due diligence. I have worked in the sector for 25 years and from every angle, as a group operator, a technology vendor, an investor-side adviser, a regulator-facing leader and a proprietor. I have run a PE-backed national group with a £98m P&L across more than 100 settings, scaled a mid-sized group, led an early years software platform from seed to Series A, and I co-own a single-site setting rated Outstanding by Ofsted, which is making its own submission separately. Cost per funded hour is the centre of my professional work, so this response concentrates on your second and fifth themes, affordability and funding, and cost drivers and provider types.

The arithmetic

The core numbers are not in dispute. The national average funding rate for a three and four year old in 2026-27 is £6.42 per hour, delivery cost for that age group in most group settings sits around £9, and the Early Years Alliance puts the average shortfall at £2.61 per funded hour, up from £2.36 a year earlier. The Department for Education's own May 2026 analysis found a median income-to-cost ratio of £1.01, with just under half of providers not covering their costs. Staffing is 70% to 80% of a typical cost base and has been rising at roughly 15% a year against funding uplifts of around 4% to 5%, driven by the National Living Wage and the 2025 employer National Insurance changes. None of this will be new to the study team, so I will concentrate on the mechanism that connects those numbers to the outcomes the study is examining.

The mechanism

A setting's viability is the gap between its delivery cost and what an hour pays, multiplied by its mix of funded and private hours. The funded rate sits below cost for most providers, so every funded hour is delivered at a loss, and the loss is recovered, where it can be, from private fees and permitted charges. That recovery is only available where families can pay. In an affluent catchment the private income covers the funded shortfall and the setting survives. In a deprived catchment the funded share of hours can reach 80% or 90% and there is no private income to recover from, so the same operator, running the same model to the same standard, loses money in direct proportion to how deprived its families are. Provision then exits the areas the entitlement was designed to reach, and new capacity opens where private demand

exists. The Department's 2025 parent survey shows the demand side of the same pattern, with 84% of under fours in households earning £65,000 or more in formal provision against 47% in households under £20,000.

What this means for the ownership analysis

This bears directly on the provider types workstream. Private equity backed groups site new openings where cross-subsidy exists, not because ownership changes the economics but because the economics reward it, and the not-for-profit and partnership settings that historically served low-income catchments on thin margins were the first to close when the wage floor rose. Places in not-for-profit settings fell 8% and in partnership settings 28% between 2018 and 2024, while private equity's share of places doubled. In my view the study will find that ownership patterns are largely an effect of the funding design rather than an independent cause of the outcomes, and the analysis should control for funded-hours share and catchment deprivation before drawing conclusions about provider type.

The charging rules

There is also an internal contradiction in the current design. The Department's guidance restricts what can be charged around a funded place and requires opt-outs and itemised invoices, yet the funding rate is only sufficient for settings that make those charges, and the Department's own position on school meals concedes that the hourly rate does not provide for them. Providers that follow the spirit of the guidance carry the cost of doing so.

The behavioural response is already visible

The Department's provider survey published in June 2026 found that over a third of group-based providers have reduced or plan to reduce three and four year old places to accommodate the expanded entitlement. That is providers rationing the loss-making product, and it is why headline place numbers can grow while availability in specific catchments falls.

What the study should measure

My main recommendation is about measurement. Filed accounts are aggregated and a year or more old, and surveys collect sentiment. The unit that decides every outcome in this study is cost per funded hour at setting level, by age band, set against the applicable local authority rate and the setting's true funded mix. That data exists inside providers' operational and payroll systems and can be assembled without much burden. If the study publishes delivery cost against funding at that level, as the launch webinar indicated it may, it will do more for the sector's understanding of itself than any single recommendation, because most providers cannot produce that number today and most policy is made without it.

I would welcome the chance to contribute to that work, through roundtables or directly, and I am willing to share the methodology I use with operators and investors.

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