CDE IN DEPTH

INVESTING IN POTENTIAL

The Financial Viability of Low-Fee Private Schools in South Africa

Executive Summary

July 2015

The Centre for Development and Enterprise, South Africa's leading development think tank, focuses on vital national development issues and their relationship to economic growth and democratic consolidation. Through examining South African realities and international experience, CDE formulates practical policy proposals for addressing major social and economic challenges. It has a special interest in the role of business and markets in development.

Series editor: Ann Bernstein

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This report, as well as the background report, is available on the website www.cde.org.za

Cover: School pupils from a township (Photo by Gallo Images)

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Low-fee private schools (officially known as 'independent schools') are growing rapidly in South Africa. In its 2015 report, *Low-Fee Private Schools: International experience and South African realities*, the Centre for Development and Enterprise (CDE) estimated that low-fee independent schools, charging annual school fees of less than R12,000,[1] are educating an estimated 250,000 learners across the country. These schools provide access to good education where there are no, insufficient or dysfunctional public schools in disadvantaged communities.

The growth of the independent school sector has been fuelled in recent years by the emergence of for-profit and not-for-profit chains of independent schools at all fee levels. The increasing interest of donors and investors in 'affordable' independent schools has given rise to important questions: Is it worth investing in low-fee independent schools? How financially viable are they? What is needed to ensure they offer quality education?

This report presents the findings of CDE's analysis and modelling of the financial viability of low-fee independent 'stand-alone' schools and chains of schools to determine the key factors that influence financial viability and what interventions might assist in this process. 'Financially viable' is defined as a school's or chain's ability to generate sufficient income to meet its operating expenses and other financial obligations, while 'sustainable' is used to mean financially viable over the longer term.

CDE's researchers obtained rich qualitative insights and financial information from visits to 23 registered stand-alone, low-fee independent schools. In addition, financial information from four chains of schools was analysed. This enabled the development of cost models, using both public and independent school benchmarks.

KEY FINDINGS

CDE's analysis and modelling found that:

- **The state subsidy is critical for the financial viability of low-fee independent schools**. Their main sources of income are the school fees, government subsidy, and donations in the case of a lucky few. The state subsidy is limited to not-for-profit independent schools that serve disadvantaged communities.[2] Schools that qualify are subsidised according to a sliding scale. Based on the level of their published fees, they can obtain between 15 and 60 per cent of what a province spends on the education of a public school learner (some R12,000 a year in 2014).[3] To obtain a 60 per cent subsidy the school fees have to be below R6,000 a year, and between R6,000 and R12,000 for a 40 per cent subsidy.
- **Independent schools that charge fees below R6,000 a year are typically survivalist**, living from month to month, not knowing whether they will be able to meet their financial obligations. Those that qualify for a state subsidy are heavily dependent on it being paid in full and on time.
- **Two types of 'hypothetical' low-fee schools are financially viable**: a 'no-frills' primary school offering a good but basic education, and an innovative secondary school delivering quality schooling through a blend of classroom teaching and online learning.
- **Stand-alone low-fee schools would be viable if they are not-for-profit and obtain a state subsidy**. These schools would need to charge fees of R11,700 a year (2013 fees), obtain a 40 per cent subsidy, and enrol some 600 to 700 learners by the third year of operation. This will enable them to repay a loan of some R30 million at 5 per cent interest over 20 years.
- **Economies of scale make a significant difference to operational costs of low-fee schools**. If this hypothetical school is part of a chain of three schools with centralised administration, it could reduce costs and would be more viable. School size matters: a large learner enrolment makes a school more cost-effective.

- **A for-profit chain of ten schools** charging fees of R11,700 per annum, with over 600 learners in each school and centralised administration, would be viable and able to cover the finance costs of a R30 million loan at 5 per cent interest over 20 years.
- **The modelling indicates that low-fee financially viable independent schools could provide better value for money than public schools in terms of a lower operating cost per learner**. Even with lower learner:educator ratios, the operating cost per learner in the 'no-frills' independent primary school is lower than in a primary public school. With a learner enrolment of 720, the operating cost per learner of the independent primary school is R12,413 per annum as opposed to the average operating cost of a learner in a public primary school of R15,955 per annum. In the case of the innovative low-fee secondary school, its per capita operating cost is lower than both the independent and public primary schools.
- **The majority of the sample of 23 stand-alone low-fee schools had existed for a long time**, although they did not necessarily meet the requirements of CDE's hypothetical models. The CDE models were based on conservative cost assumptions to strengthen their financial viability. In reality, low-fee schools survive because they are located in basic premises, which they do not own, are poorly resourced, pay low teacher salaries, and in some cases receive donations. Typically they have never taken out a loan.

CHALLENGES AND RISKS

CDE's analysis identified considerable challenges and risks in establishing and sustaining low-fee independent schools:

- **The regulatory environment is increasingly disabling**. The complex maze of legislation from all sectors of government impedes the establishment of new schools and imposes very high compliance costs which low-fee independent schools struggle to meet. More accountability (with severe sanctions for non-compliance) is demanded from independent schools than public schools.
- **The lack of capacity in government departments and statutory bodies** results in delays in registration, payment of subsidies, and accreditation. If a new school does not become registered in good time or the subsidies are reduced or late, the cost of establishing and running a low-fee school increases significantly.
- **Securing affordable premises** is one of the greatest challenges for low-fee independent schools.
- **The lack of access to loan finance at affordable interest rates** prevents them from expanding to a cost-effective size, buying or building new premises.
- **A high turnover of teachers** results from low salaries.
- **Timely and full payment of school fees and subsidies, tight control over income and expenditure, high learner enrolment, and quality teaching and learning** are key to a school's financial viability.
- **The selection of the right principal and teachers is the 'secret sauce'**, critical for the success of the school. They have to embed a values-based ethos, establish sound discipline, and set high academic standards.
- **Low-fee independent schools wrestle with a perpetual tension between school fees, access for poor children, and quality**. If the fees are set higher, fewer parents will be able to enrol their children, but the quality is likely to improve. If the fees are too low, the quality of education and the viability of the school will be at risk.

CDE RECOMMENDATIONS

To enable low-fee schools to become more financially stable and provide affordable, good quality education to even poorer communities, CDE proposes a number of reforms by government and interventions by the private sector.

Government reform

- Simplify the legislation governing independent schools, remove duplicative processes, and develop more supportive policies that still ensure sufficient accountability. All these would reduce the heavy compliance costs for both the schools and government departments/bodies.
- Increase the level of state subsidy per learner in not-for-profit low-fee independent schools. This reform would enable them to decrease their fees and serve poorer communities, at a lower cost to government. The 2006 National Norms and Standards for School Funding (as amended in 2008) make provision for a provincial Member of the Executive Council (MEC) to increase the subsidy level in consultation with the Department of Basic Education.

Private interventions

Corporate investors and donors can increase the viability of low-fee independent schools in many ways. They can:

- Advocate a more enabling policy framework that would reduce regulatory requirements and costs and increase subsidies through policy engagement with government at national and provincial levels and in stakeholder forums, such as the National Education Collaboration Trust.
- Establish growing numbers of innovative and cost-effective low-fee schools and chains.
- Provide affordable loan finance to new or expanding schools, with a grace period before repayment begins, so the school can reach a cost-effective size.
- Widen the dominant focus of corporate social investment (CSI) on public schools to include support for low-fee independent schools. This could involve assisting the development of new low-fee schools; strengthening existing ones to become registered, accredited and financially viable; and supporting the piloting of innovations.
- Make technical expertise available to enable schools to develop sound strategic and business plans, establish financial and administrative systems, and acquire appropriate technology.
- Fund a school position for an instructional leader, such as an academic deputy-head, to strengthen academic quality.
- Fund additional research and advocacy interventions to support regulatory reform, innovation, quality assessment, and cost-effectiveness.

CONCLUDING REMARKS

CDE's modelling points to the potential of low-fee independent schools to provide affordable, good schooling to poor communities on a sustainable basis. The research has identified viable financial models of stand-alone and chains of low-fee independent schools that could be of benefit to investors, 'edupreneurs', donors, the independent school sector, and ultimately the country.

In the context of a struggling public schooling system, the development and expansion of independent schools serving poorer communities is a positive trend that needs greater support and a more enabling policy environment. It is in South Africa's interests for low-fee schools to reach even poorer communities. For this to happen subsidies should be higher and compliance costs reduced so that schools are able to charge lower fees and sustain quality education.

This is an executive summary of a CDE Report, INVESTING IN POTENTIAL: :
The Financial Viability of Low-Fee Private Schools in South Africa. The full-length publication can be downloaded from www.cde.org.za.

ENDNOTES

1. CDE defines low-fee schools as those that charge fees below R12,000 per annum, which roughly equates to the 2014 national average of provincial expenditure per learner in a public school.
2. Department of Basic Education, South African Schools Act No. 84 of 1996: National Norms and Standards for School Funding (as amended in 2008) (Pretoria: DBE, 2008).
3. No high-fee or for-profit independent school can qualify for a subsidy.

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