COVID-19 and the challenges facing childcare in England

Christine Farquharson, Institute for Fiscal Studies
Megan Jarvie, Coram Family and Childcare
Gillian Paull, Frontier Economics
Childcare during the lockdown

Christine Farquharson, IFS

4 September 2020

@TheIFS
Childcare during the lockdown

% of settings open (right axis)

Children attending (left axis)

Source: Department for Education statistics. See Figure 2.1, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England” for full sources.
Childcare during the lockdown

Since 1 June, all children allowed to return to childcare

Source: Department for Education statistics. See Figure 2.1, "Challenges for the childcare market: the implications of COVID-19 for childcare providers in England" for full sources.
Since 1 June, all children allowed to return to childcare

% of settings open (right axis)

Children attending (left axis)

Source: Department for Education statistics. See Figure 2.1, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England” for full sources.
Government support since March

Support depended on the source of income and the type of provider

- **Public funding** (for the free entitlement) continued as normal
- Employers with lost income from parent fees could **furlough** staff
- **Self-employment grants** for childminders with lost income

There were also a number of other sources of support

- Business rates holiday
- Extensions to universal credit
- Small business grants, gov’t-backed loans, VAT deferrals, local authority support packages
Government support since March

2018 income sources

- 64% Parent-paid fees
- 27% Free entitlement funding
- 11% Other income

- Income from free entitlement funding protected
- Other income (e.g. LA grants) also mostly protected
- Childminders (mostly) get some extra lockdown income via SEISS
- Income from parent-paid fees at risk during lockdown

Source: Cattoretti, Paul and Marshall (2019); see Figure 3.2, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England” for full sources.
Government support since March

- For group-based providers, staff costs largely covered via furlough scheme
- Most other costs remained during lockdown

2018 cost breakdown

- Staff: 72%
- Rent/mortgage: 13%
- Food and materials: 13%
- Other: 8%

Source: Cattoretti, Paull and Marshall (2019); see Figure 3.3, "Challenges for the childcare market: the implications of COVID-19 for childcare providers in England" for full sources.
Providers’ finances during lockdown

- Detailed information about providers’ income and costs from a nationally representative survey in 2018
- We model what providers’ finances might have looked like under two lockdown scenarios:
  - “No-fee” lockdown: All income from parent fees disappears
  - “15% fee” lockdown: Providers retain 15% of their fee income
- Both scenarios incorporate continued public funding and support via furlough and self-employment schemes
- We assume providers are still responsible for all other costs
Income-to-cost ratios during lockdown

Source: Figure 4.2, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England”, IFS Report R175.
Income-to-cost ratios during lockdown

Source: Figure 4.2, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England”, IFS Report R175.
What drives differences between provider types?

Source: Figure 4.3, "Challenges for the childcare market: the implications of COVID-19 for childcare providers in England", IFS Report R175.
What drives differences between provider types?

1. Pre-crisis finances

2018 ICR for providers in deficit in ‘no fee’ lockdown

- Significant surplus
- Middle group
- Already in deficit

Source: Figure 4.3, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England”, IFS Report R175.
What drives differences between provider types?

1. Pre-crisis finances

2. Different sources of funding

Source: Cattoretti, Paull and Marshall (2019); see Figure 3.2, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England” for full sources.
What drives differences between provider types?

1. Pre-crisis finances
2. Different sources of funding
3. Extent of gov’t support

% of baseline fee income replaced by furlough/SEISS

© Institute for Fiscal Studies

Source: Figure 4.5, “Challenges for the childcare market: the implications of COVID-19 for childcare providers in England” for full sources.
Summing up

- Providers saw a significant financial hit from the lockdown
  - Twice as many private nurseries now in significant deficit

- It would have looked a lot worse without government support.

- Providers relying on income from parent fees were less well protected
  - Private providers and childminders have been harder hit; nursery classes less so
Challenges for the childcare market: the implications of COVID-19 for childcare providers in England

Dr Gillian Paull

4th September 2020
What might happen going forward?

We now consider:

• What might happen to providers’ finances as Government support ends and parent demand may (or may not) recover.

• Longer term risks to the market and the nature of provision.

• Why and how Government might intervene to support provision.
Two sets of key challenges in the next few months

End of Government support

- Furlough scheme being wound down before ending on 31st October
- Final SEISS payment in August covering three months (end October)
- Free entitlement funding will be based on attendance from January 2021 (rather than pre-crisis child numbers)

Recovery of parent demand

- Recovery of demand
  - Furlough scheme ending + call for workers to return to the workplace
- Lower demand than pre-crisis
  - Health related concerns for children
  - Higher unemployment
  - More parents working at home
We have estimated the possible impacts on providers’ finances

We use “scenario modelling”:

• Know what will happen to Government support.

• But we don’t know what will happen to parent demand - consider a range of possibilities for fee income and free entitlement funding.

• Assume no immediate adjustment in costs.

Use the same data and ICR (income-to-cost ratio) as we used for the lockdown estimates:

• Furlough and SEISS support removed.

• Test impacts of lower fee income in five increments: 5%, 10%, 15%, 20% and 25% losses.

• Test impacts of lower parent-paid fee income and free entitlement funding.
How are providers’ finances affected under different scenarios of lower fee income?

- Baseline is pre-COVID.
- Every 5% increment in lost income additional 3-4% in significant deficit.
- Under central scenario of 15% fees lost: increase from 28% to 38% in significant deficit.
And under different scenarios of lower fee income and free entitlement funding?

- Baseline again is pre-COVID.
- Every 5% increment in lost income additional 4-6% in significant deficit (compared to 3-4% for fee only loss).
The impacts vary across different types of providers

Private providers - lost fees and funding have similar impacts

Childminders - lost fees have much bigger impact

Voluntary providers and nursery classes - lost funding has much bigger impact

Reflects the differences in income sources across provider types
**What are the longer term challenges for childcare providers?**

<table>
<thead>
<tr>
<th>Demand challenges</th>
<th>Managing delivery with COVID-19</th>
<th>Future local or national lockdowns</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recovery of losses from lockdown</td>
<td>Staffing restrictions / absences could increase costs</td>
<td>No furlough scheme or SEISS</td>
</tr>
<tr>
<td>Permanent income loss if demand does not recover</td>
<td>Limited interaction with parents could inhibit new business</td>
<td>Continued free entitlement funding could support only some providers</td>
</tr>
<tr>
<td>Changes in demand for different types of childcare</td>
<td>Limited interaction with specialist staff could reduce care quality</td>
<td>Risk of lockdowns without Government supports could impact on investment</td>
</tr>
</tbody>
</table>
### How might providers respond?

<table>
<thead>
<tr>
<th>Fee increases for parents:</th>
<th>Adjustments to business models:</th>
<th>Reduced capacity:</th>
</tr>
</thead>
<tbody>
<tr>
<td>To make up income shortfall</td>
<td>To revive sustainability</td>
<td>To align with lower demand for the sector</td>
</tr>
<tr>
<td>Quick / simple change</td>
<td>Change mix of parent-paid and funded hours</td>
<td>Providers offer fewer hours or fewer places</td>
</tr>
<tr>
<td>May be limited by parents’ inability to pay more during economic downturn</td>
<td>Switch provision to more profitable children (by age / child needs)</td>
<td>More settings close and / or fewer open than pre-crisis</td>
</tr>
<tr>
<td>Less feasible in less affluent areas and those more affected by economic downturn</td>
<td>Switch to lower cost staffing (less qualified)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Reduce flexibility of hours to reduce costs</td>
<td></td>
</tr>
</tbody>
</table>

Quick / simple change may be limited by parents’ inability to pay more during economic downturn. Less feasible in less affluent areas and those more affected by economic downturn.

Providers offer fewer hours or fewer places. More settings close and / or fewer open than pre-crisis.
Should the Government intervene?

Government already intervenes
Free Early Education Entitlement, Tax Free Childcare, Employer Vouchers, WTC/Universal Credit childcare, LA sufficiency duties.

To support child development:
• Parents underestimate benefits
• To address socio-economic inequalities

To support working parents:
• Particularly mothers (gender equality)

Will the market optimally adjust to the new demand and cost conditions?

Existing reasons may be more important:
• Possible declines in quality or flexibility
• Educational benefits hidden under health concerns
• Loss of childcare harmful for more disadvantaged children

Or does the sector now need additional support?

To support specific parts of the market:
• Reduced access in some communities or for some children
• To ensure continued delivery of free entitlement
What options could the Government consider?

Support during further lockdowns
E.g. continued free entitlement funding, temporary grants / furlough schemes.

Transition funding for new COVID-19 requirements
E.g. grants for providers to cover the costs of one-off adjustments

Boosting income from parent-paid fees
E.g. public campaign on safety of childcare and benefits of early education
E.g. increasing subsidies in Tax Free Childcare or Universal Credit

Boosting public income
E.g. increasing free entitlement funding rates (although limited support for providers hit hardest during lockdown)
E.g. increasing supplements for some children (disadvantaged or those with special needs)

Reducing start-up costs
E.g. offering start-up capital, reducing the costs of Ofsted registration

Reducing ongoing delivery costs
E.g. relaxing maximum child-staff ratios (although could affect quality)

Investing in maintained provision
E.g. encouraging more nursery provision in schools to create more stable capacity
Conclusions

• Greatest challenge for the childcare market going forward is whether parent demand for childcare will recover to pre-crisis levels:
  • Childminders face the greatest loss of income from parent-paid fees.
  • But voluntary providers and nursery classes will be harder hit if take-up of free entitlement places does not return.

• Is increased Government intervention needed going forward?
  • Maybe not - childcare market can sustain significant levels of provider turnover and has shown an ability to adapt to a changing environment.
  • Higher funding rates could help ensure uninterrupted delivery of the free early education entitlements.
  • However, hardest hit providers may be those more reliant on parent-paid fees → suggests a range of other policy options may be more effective to help the childcare market meet the challenges of COVID-19
Frontier Economics Ltd is a member of the Frontier Economics network, which consists of two separate companies based in Europe (Frontier Economics Ltd) and Australia (Frontier Economics Pty Ltd). Both companies are independently owned, and legal commitments entered into by one company do not impose any obligations on the other company in the network. All views expressed in this document are the views of Frontier Economics Ltd.