

# Private investment in independent schools

## Conclusions

- Accumulated profits between 2006 and 2010 totalled almost SEK 820 million
- External funding via borrowing amounted to approximately SEK 2,200 million
- New share issues over the period amounted to SEK 774 million and an in-depth study covering 2000-2006 gave a further approximately SEK 200 million
- Total investment amounted to SEK 2,004 million
- Dividends paid amounted to approximately SEK 30 million

## Introduction

The purpose of this memorandum is to address an issue of topical interest in the social debate – independent schools' profits.

The independent school companies are today accused of realising high profits and that taxpayers' money is thereby finding its way into private business people's pockets without necessary investments being made.

This review puts this in relation to what the companies invest in their business – in relation to both operating profit and employed external capital.

## Method

**Scantech Strategy Advisors**, commissioned by Almega, have examined the annual reports of the ten largest independent school groups over the five-year period from 2006 to 2010 and drawn up tables of profits, dividends, borrowing, investments, turnover and new share issues. Since the independent school reform of the 1990s the number of private alternatives in the school sector has increased and some large independent school companies, or rather educational groups, have begun to appear as a result of some of the companies growing through reinvestment of their profits or through external capital being brought into the business through new share issues, loans from the shareholders or loans from credit institutes. Even if the public sector funds their operation through the so-called school capitation allowance, building or taking over schools requires financial muscle. With external capital,

private players can contribute money that would otherwise not have been available in the welfare sector.

One advantage of independent schools as opposed to municipal schools is that the investment horizon can be longer than just a few years. Investments in schools naturally take the form of fixtures like furniture, equipment for teaching and premises but also pedagogical concepts, acquisition or establishment of schools and further education for the staff.

Investments are as a rule funded through:

- Reinvestment of profits
- Borrowing from banks or other credit institutes
- New share issues where new capital is provided by existing and new owners

Several of the companies are groups with one or more subsidiaries. In those cases we have looked at the transactions of the group and/or the parent company. Group accounts have primarily been used but where an individual subsidiary has been responsible for the educational side of the business, its accounts have been used instead.

Some of the companies have not drawn up any cash flow analyses at any time during the period and it has thus been difficult to form a comprehensive picture of the individual companies. This means that it has been difficult to attribute investments and borrowing and the figures may therefore be underestimated.

The ten companies in the analysis are the following: AcadeMedia, John Bauer, Engelska skolan, Kunskapsskolan, Baggium/Praktiska, Pysslingen, Jensen, Thorengruppen, PPS and Prolympia.

## **Analysis**

- It is quite clear that external financing via borrowing and new share issues vastly exceeds the profits distributed.
- The companies manage their investment needs by reversing profits and borrowing. This establishes a long-term commitment that is often lacking in the public sector.
- The industry shows the same trends as the rest of Swedish trade and industry, where companies grow through declining to realise profits and/or traditional borrowing. This is clear from among other things SEB's Entrepreneur Panel (Q4 2010), where 37% of the companies state that they go to their bank for funding, only 2% to venture capital companies and all of 55% that they have not sought external funding.

**The premise that constitutes the basis** for this memorandum is to study annual reports to determine how much external capital is brought into the businesses. Much of the expansion that takes place in the independent schools is funded by reinvestment of profits. This is common in a Swedish trade and industry context since the proportion of venture capital is relatively small. As regards new share issues, only AcadeMedia have made one of any substance. External funding through borrowing is more more common, as can be seen from the matrix at the end of this memorandum.

Investment levels are distinctly higher than profits over the period. The companies have borrowed money in different ways. John Bauer for example has borrowed SEK 200 million from its shareholders. Prolympia has borrowed SEK 20 million in the same way. Other companies have borrowed from credit institutes. Only borrowing from credit institutes appears in the tables.

The total profit over the period amounted to SEK 817 million while investments totalled SEK 2.4 billion. A total of approximately SEK 678 billion was borrowed in the form of new loans and new share issues gave SEK 774 million.

Together with accumulated profits this is largely on a par with investments made. In relation to the total dividends paid of approximately SEK 30 million, the conclusion can also be drawn that the companies' equity has improved considerably over the period.

**New share issues are relatively rare** so a more in-depth study was made of the 2000-2005 period, where more new share issues by AcadeMedia and Kunskapsskolan were found, which raised a total of SEK 205 million for the two companies. For several years at the beginning of the decade, both AcadeMedia and Kunskapsskolan reported a loss. This is a factor to take into account in one's standpoint as regards profits in the independent school sector. Some degree of perseverance is needed to get any return on capital invested.

Dividends are fairly rare and lower than what comes out in the public debate. John Bauer, which during the period has reported a loss, has been forced to use its equity to cover the deficit at the same time as the business has expanded substantially. The picture in the public mind of an independent school being a land of milk and honey is therefore misleading.

From a purely academic perspective, the empiric data shows that independent schools produce higher quality at a better price for the taxpayer. This is true not only in terms of money per grade credit, but also, which is an important and generally better result in national tests, when adjusted for factors such as socio-economic background which

could be a contributory cause. Financial efficiency is among other things due to pupil-teacher ratios in general being lower in independent schools than in publicly run schools. There is no clear correlation between pupil-teacher ratio and grades; it is other factors that play a major role according to the Swedish National Agency for Education and others involved in school research.

More figures are available from the National Agency for Education and the Swedish Association of Independent Schools. One advantage that independent schools have compared to publicly run schools is that they can plan their finances in the long-term. They are not dependent on the strict budget rules of the Local Government Act. A positive result one year can be carried over to the following year and thus form a foundation for future investments, while publicly run schools must depend on political decisions. This is unusual – especially in times of economic austerity. The opposite also applies. Since the companies often carry forward positive results they can handle years with less good results without needing to make substantial cutbacks. Another aspect is that the incentives to achieve positive results are poor in municipal schools for two reasons: 1) any surplus risks being clawed back by the local authority and 2) a positive result may lead to a smaller allocation the following year. At the end of the years it can thus be suspected that money is used in order for a surplus not to signal a need for a lower allocation. This rarely leads to long-term investments.

#### **Summary 206-2012 (millions)**

	Dividends	Profits	Investments	New share issues	Borrowing
Engelska skolan	2.2	86	264.5	0	0
Pysslingen	6.1	110	174	0	78
Baggium/ Praktiska	15.5	130	80	0	21.5
John Bauer	1	-124	496	0	351
Jensen	1	132	32	0	0
Thoren- gruppen	1.69	9	10	0	10
PPS	3.5	23	60	0	2
AcadeMedia	0	350	1,077	774	225
Prolympia	0	-39	31.5	0	16
Kunskaps- skolan	0	140	178	0	-25
<b>TOTAL</b>	<b>30.9</b>	<b>817</b>	<b>2,403</b>	<b>774</b>	<b>678.5</b>

In the summary above, the five latest annual reports per March 2012 have been used. This means that the figures for some companies are for the period between 1 January 2006 and 31 December 2010 and for others the period from 1 July 2006 to 30 June 2011. A few of the companies have changed their financial year and thus have a measurement period that is 6 months shorter.

## The companies

The tables below show the turnover for the accounts closed in 2010. This means that some of the companies use a split financial year and their annual turnover thus refers to the period from 1 July 2009 to 30 June 2010. In one or two cases this switch takes place during the measurement period, which means that the measurement period for these companies is six months shorter.

## AcadeMedia

AcadeMedia is by far the largest of the independent school groups. In 2011 Pysslingen, among others, became a member of the group, making AcadeMedia more than twice as large as the next largest company in the industry. Between 2006 and 2010 the company underwent substantial expansion with increased turnover. This expansion was achieved through acquisition of already existing independent schools.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
AcadeMedia	350	1,077	774	225	0

**Turnover 2010: SEK 1,231 million\***

\* Reports 2010 as a half-yearly closing, which means that the turnover above refers only to six months.

## John Bauer

Like AcadeMedia, John Bauer consists of several subsidiaries. Over the five-year period the business expands substantially and turnover increases from 266 to SEK 1,267 million. The parent company shows a profit but looking at the group's results, the consolidate accounts show a loss.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
John Bauer	-124	496	0	351	1

**Turnover 2010: SEK 1,267 million**

## Engelska skolan

Over the measurement period Engelska skolan shows a steady profit and fairly small dividends. This is probably due to the ownership structure, where the founder still owns 100% of the company. The company grows by reinvesting its profits.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Engelska skolan	86	264.5	0	0	2.2

**Turnover 2010: SEK 500 million**

## Kunskapsskolan

Like Engelska skolan, Kunskapsskolan's growth strategy is to grow through reinvestment of profits. There were no new share issues over the measurement period but the company began operating in 2000 and was funded through new share issues which raised SEK 75 million over three years. No new issue was made during the period examined but group contributions were paid to the parent company, which does pay dividends.

Kunskapsskolan is owned by Kunskapsskolan Education Sweden AB. The analysis of Kunskapsskolan i Sverige reveals no external funding through borrowing. In the accounts for the 2008 financial year, the group including the parent company Kunskapsskolan Education Sweden AB posts debts to credit institutes of approximately SEK 200 million and debts to owners of SEK 103 million. Kunskapsskolan Education Sweden AB has other areas of business alongside running 9-year compulsory schools and upper secondary schools. In this case the business examined was Kunskapsskolan i Sverige AB.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Kunskaps-skolan	140	178	0	-25	0

**Turnover 2010: SEK 767 million**

## **Pysslingen Förskolor och skolor AB**

Pysslingen has largely grown through reinvestment of profits and has over the measurement period posted a total profit of SEK 110 million. SEK 174 million was invested in the business over the same period, primarily relating to starting up or taking over new schools. Pysslingen was acquired by AcadeMedia in 2011.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Pysslingen	110	174	0	78	6.1

**Turnover 2010: SEK 1,130 million**

## **Baggium**

Among other things Baggium runs upper secondary education programmes within Praktiska's framework. During the measurement period the company made a profit of SEK 130 million and invested SEK 80 million. Major changes were made to the organisation in 2008, which has made the financial analysis difficult. Dividends totalling SEK 15.5 million were paid to the shareholders.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Baggium	130	80	0	21.5	15.5

**Turnover 2010: SEK 680 million**

## Jensen Education AB

Jensen Education's total profit over the measurement period amounted to SEK 132 million and in its 2006 annual report the company wrote that growth is funded through the company's equity and that the company has no loans. This is also stated in the annual reports for 2007-2010. Over the period dividends of only SEK 1 million have been paid to the shareholders.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Jensen	132	32	0	0	1

**Turnover 2010: SEK 350 million**

## Prolympia

Over the period Prolympia made a loss of SEK 39 million, which has been covered by a conditional owner's contribution. Investment was funded by loans that were later repaid in 2010. The total amount borrowed over the period was SEK 16 million. The company is a wholly-owned subsidiary of Rubato, which in turn is owned by Ted International Holding AB.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Prolympia	-39	31.5	0	16	0

**Turnover 2010: SEK 102 million**

## Thorengruppen

Thorengruppen has shown strong growth over the period. In their annual report for 2010 they say themselves that expansion should be able to take place through its own dynamism. No cash flow analysis was made between 2006 and 2009 and it is difficult to look more closely at investments and funding. SEK 10 million was however invested in 2010 and it can be seen from the financing activities that this was done without taking up new loans.



**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
Thorengruppen	9	10	0	10	1.69

**Turnover 2010: SEK 142 million**

## **PPS AB**

PPS runs and develops 9-year compulsory schools and upper secondary schools, including Cybergymnasiet and Donnergymnasiet. PPS' operations are purely educational and are relatively small compared to those of other companies in the study. A cash flow analysis exists only for the last year and it is not easy to make a deeper analysis of investments and borrowing.

**Table: Development 2006-2010 (millions)**

	Profits	Investments	New share issues	Borrowing	Dividends
PPS	23	60	0	2	3.5

**Turnover 2010: SEK 290 million**