An Independent Review of Financial Strength and Adaptability of Anglo Skills College Ltd

Report Produced By:

Dynamic Financial Services Limited

Report Submitted To:

Senior Management Committee, Anglo Skills College

Acccountants & Business Advisors

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Yours faithfully,

Dynamic financial Services

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2. Introduction

Background

The Senior Management Team of Anglo Skills College (ASC) had commissioned this independent external Review of its financial strength and adaptability and had appointed Dynamic Financial Services (DFS) to review it. The Review's mandates are to assess current financial strengths of ASC, assess any symptoms of overtrading and whether it is financially adaptable under different business scenarios. We take this as a commitment by ASC to be satisfied that its financial performance is in line with HE sector and regulatory standards.

Sources

The data used in this report come from three main sources.

a. Data up to and including 2017-18 for Universities are from the Higher Education Statistics Agency's Finance Statistics Record, which is completed by all institutions each year.

b. Audited accounts for the College "Anglo Skills College Limited" for the year ended 28 February 2018 and 2019 and management accounts for the period ended 31 January 2020.

Approach to the Review

In compiling this report, we conducted independent analysis of internal data as well as external data.

Internal data included the financial data submitted to the Office for Students, audited financial statements and management accounts for the period 31 January 2020.

External data included annual audited accounts (including financial statements), various HEFCE reports (such as financial health of the higher education sector); regulatory requirements and guidelines; HE sector reports, books and database analysis.

We used various data and compared the College data with that of financial data available for HE sectors.

Financial statements have been interpreted using ratio analysis and then findings have been benchmarked against the data published by HESA for HE Institutes. This will provide an insight into the financials for the college as compared to HE & other OfS registered institution.

Acknowledgement

We would like to formally extend our thanks to the members of the College's Senior Management Team (SMT), staff and employees together with the members of the statutory auditors and external accountants for the assistance they have given us during the review.

3. *Financial Performance*

Our review of the financial statements shows that the financial position of the College has significantly improved for the period ended 31 January 2020. Overall net profit before tax increased to £41,829 (30.9% percent of income) as compared to £11,144 (13.6% percent of income) in the previous year.

The improved financial results arise principally from increases in Academic and General English student numbers, which increased from 13 students to 24 and also due to its better margin than usual IELTS courses.

The balance sheet has significantly improved from a position of total net assets of £7,372 to £44,634. This increase is mainly driven by the strong performance in Jan 2020. Cash reserves increased significantly by 4.33 times to £27k (61.4% of current assets) from the 2019 position of £6k (85.2% percent of current assets).

Cash flow from operating activities also increased to £35k (25.9% of income), compared with £6k (7.4% of income in 2019). The increase is mainly driven by the delivery of higher margin courses mainly Academic and General English course contracted with the Saudi Arabian Government.

4. Financial Ratio Analysis

Ratio analysis is a useful management tool that helps in understanding the financial results and trends over time, and provides key indicators of organizational performance.

We have calculated ratios into four major categories:

- Profitability Sustainability
- Operational Efficiency
- Liquidity
- Leverage (Funding – Debt, Equity, Grants)

Profitability Sustainability Ratios

Profitability Sustainability Ratios can be used to assess how well is the business performing over a specific period and whether the College has adequate financial resources to meet financial challenges in the short term.

We have performed the sales growth ratio as below:

a) Sales Growth

The ratio calculates the percentage increase (decrease) in sales between two time periods.

Sales growth	***2020(11 months)***	***2019***	***Change***	***% Change***
ASC	134,975	82,146	52,829	58.1%

The above ratio indicates that the revenue rose by 58.1% to £134,975 for the period ended to 31 January 2020. The significant growth is mainly due to an increase in the student numbers which grew by 25 (a 56 percent increase from the level in 2019). This indicates the fact that management is successfully implementing its strategy and is able to introduce new courses and recruit students while expanding. Due to the on-going growth this percentage is expected to increase in the following years.

b) Return on total assets

This ratio measures institution's ability to turn assets into profit.

Return on total assets	***2020 (11 months)***	***2019***	***% Change***
ASC	56.3%	69.5%	-13.2%

The above decrease of 13.2% year-on-year indicates that the assets utilization has declined. This ratio is slightly distorted due to the fact that in 2019, the college didn't have this number of course or students studying as at period end and carried a significantly lower fixed assets, debtor and cash balances. During the year, the college has invested in fixed assets and have significantly higher cash and debtor balances. The debtor balance is expected to reduce by the year end i.e. 29 February 2020, as it is slightly distorted due to 11 months period. Although, the percentage has decreased but it still shows a strong utilization percentage of over 50%, which is indicative of the fact that the College is managing and utilizing the assets efficiently.

c) *Gross profit ratio*

This ratio is used to assess institution's financial health by revealing the proportion of money left over from revenues after accounting for the cost of services or direct cost provided. Gross profit margin serves as the source for paying additional expenses and future savings.

Gross profit ratio	2020 (11 months)	2019	% Change
ASC	76.13%	71.94%	4.19%

The above again indicates, College's delivery of better margin courses, as even with the significantly increased revenue, the college has achieved a better gross profit margin. This indicates that even with significant growth the college can manage and deliver improved financial results.

d) *Net profit ratio*

This ratio is used to assess institution's financial health by revealing the proportion of money left over from revenues after accounting for the total costs. In other words, it measures how much out of every pound of revenue an institution actually keeps in earnings. A higher profit ratio indicates a more profitable institution that has better control over its costs.

Net profit ratio	2020 (11 months)	2019	% Change
ASC	30.9%	13.6%	17.4%

The above ratio shows that the College has significantly improved its profitability and managing its operation well in expansion phase.

Operational Efficiency

Operational efficiency ratios indicate how efficiently an institution utilises its assets and manage its liabilities. These ratios are used to compare performance over multiple periods.

a) *Operating expense ratio*

This ratio compares expenses to revenue. A decreasing ratio is considered desirable since it generally indicates increased efficiency.

Operating expense ratio	2020(11 months)	2019	% Change
ASC	40.84%	57.76%	16.91%

As shown above the College was able to improve its operating expenses ratio by 16.91% while increasing its revenue by 58.1%. This indicates the quality of management, while growing the College, management is also improving its operational efficiencies.

Liquidity Ratios

Liquidity ratios are used to assess whether an institution has adequate cash on an ongoing basis to meet its operational obligations. This is an important indication of financial health. The importance of this liquidity arises in the periods of significant growth as overtrading problems might occur.

b) Current Ratio

The current ratio is the measure of liquidity and compares current assets to current liabilities. It indicates whether the business can pay debts due within one year out of the current assets. The current ratio reveals how much "cover" the institution has for every £1 that is owed by the institution.

Liquidity ratio	2020(11 months)	2019	% Change
ASC	2.57	2.07	23.98%

The above ratio indicates that the College has improved its coverage of current liabilities by 23.98%. It also indicates that for every £1 of current liability the College has got £2.57 to pay off, which is considered to be a strong liquid position.

c) Quick Ratio

A more stringent liquidity test that indicates if an institution has enough short-term assets (without selling inventory) to cover its immediate liabilities. This is often referred to as the "acid test" because it only looks at the company's most liquid assets only (excludes inventory) that can be quickly converted to cash). A ratio of 1:1 means that an institution can pay its bills without having to sell inventory.

As College do not hold any inventory hence the current ratio above of 2.57 is considered to be its quick ratio, which again indicates the strong liquidity position of the College.

d) Adequacy of Resources

This ratio determines the number of months an institution could operate without further funds received (burn-rate). The measure takes into account monthly operating expenditure (no direct costs included) excluding depreciation to cash, marketable securities and accounts receivable.

	2020(11 months)	2019	Change
ASC	13.32	1.81	11.51

The above ratio indicates that the College can operate up to 13.32 months with the current levels of funds. The liquidity position with reference to months has improved significantly by 11.51 months or a change of 635.81%.

The period of 4.63 months (139 days) is considered adequate for the College in HE sectors, as indicated by the benchmarking data below. This calculation is based on the College's current level of expenditure.

Leverage Ratios
These ratios are used to assess to what degree an institution utilises borrowed money and its level of risk. Lenders often use this information to determine a business's ability to repay debt.

e) Gearing

Compares capital invested by owners/funders (including grants) and funds provided by lenders. As Anglo College is external debt free the gearing ratio is nil and as compared to the peers is in a better position as it has not got an obligation to pay interest and repayment of debt. Also, due to its debt free nature, the College has not got any covenants to meet while it is growing.

Overtrading
The condition of an entity's which enters into commitments in excess of its available short-term resources. This can arise even if an entity is trading profitably and is typically caused by financing strains imposed by a lengthy operating cycle or production cycle.'

In the case of Anglo College, it has expanded significantly over the course of 11 months to 2020. The revenue grew by 58.1% while the net profit after tax increased by 17.42% to £41.8k. We assessed whether this level of growth might has affected its ability to mitigate risks related to overtrading. We looked at whether there are any symptoms and/or conditions of overtrading exist. Using above solvency, liquidity, gearing and profitability ratios, we can report that the College has not entered into any commitments in excess of its available short-term resources. All of these ratios look favorable and are significantly above the ideal threshold levels.

We have compared the above ratio with that of the HE sector in the following section of this report. We can clearly see that even during the expansion phase the College managed to improve its liquidity position which is apparent from the increase in current/quick ratio to coverage of approx. 2.57 times (see above) of current liabilities; this should mitigate any risk of financial strains. Also as above, College have resources to operate for 13.32 months, this is considered to be a healthy indicator and above average for HE sector.

Overall, the College's liquidity position is considered to be strong, which should be able to mitigate any risk of overtrading.

5. Benchmarking

In order to further assess the financial stability of the College 'ASC', we have performed a benchmarking exercise to compare College's financial ratios to the HE sector averages. The benchmarking data is derived from the key financial indicators as published by HESA at https://www.hesa.ac.uk/data-and-analysis/finances/kfi from 2015/16 to 2017/18. As the data for 2018/19 and 2019/20 is not yet available, we have assumed the financial ratio for 2018/19 and 2019/20 to be broadly in line with the averages of the previous three years, and compared 2018/19 and 2019/20 with these averages.

Benchmarking is a very useful tool as it may highlight any issues or trends for going concern issues or identify possible risk areas.

a) Historic cost surplus/deficit after tax as a % of income

Table 1:

Surplus/(deficit) as a % of total income	2017/18	2018/19	2019/20
HE Sector	1.72%	2.94%	2.43%
ASC	(10.3%)	13.6%	30.9%

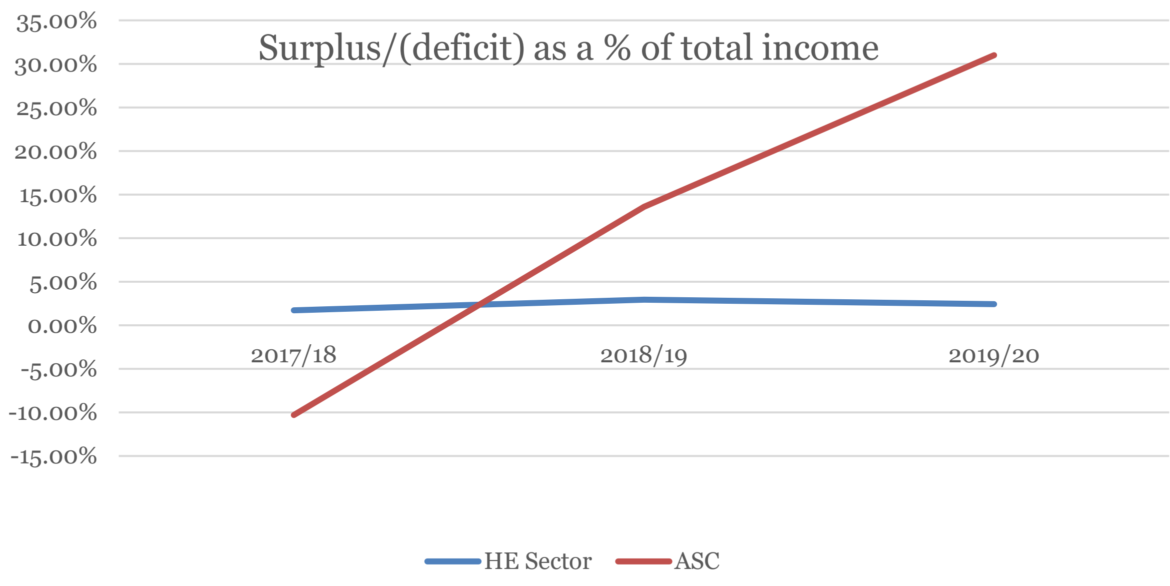


Figure 1:

Current Performance Indicator: Positive above HE Sector

Historic cost surplus/deficit after tax as a % of income is a useful tool to measure the overall profitability of the business. A high ratio indicates the efficient management of the affairs of business.

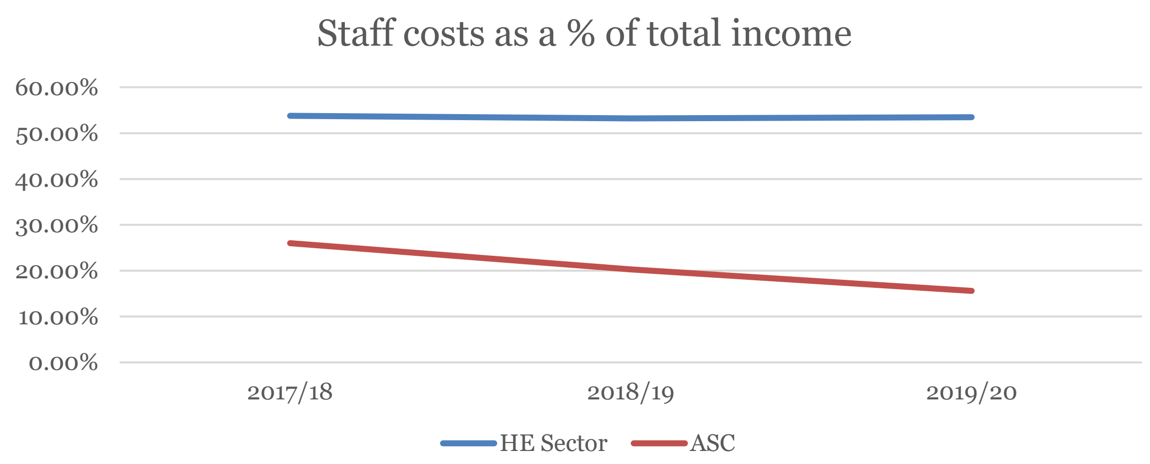
As shown above the HE sectors are averaging 2.94% to 1.72%, over the course of period. College's ratio improved significantly from -10% to 31%, currently which is significantly above the sector and indicative of the fact that College is constantly improving its profitability by the increasing its net profits margins.

b) Staff costs as a % of income

Table 2:

Staff costs as a % of total income	2017/18	2018/19	2019/20
HE Sector	53.77%	53.21%	53.45%
ASC	26.0%	20.3%	15.6%

Figure 2:



Current Performance Indicator: Positive better than HE Sector

The HE sector's biggest expenditure is staff costs, which is above 50% of the total income.

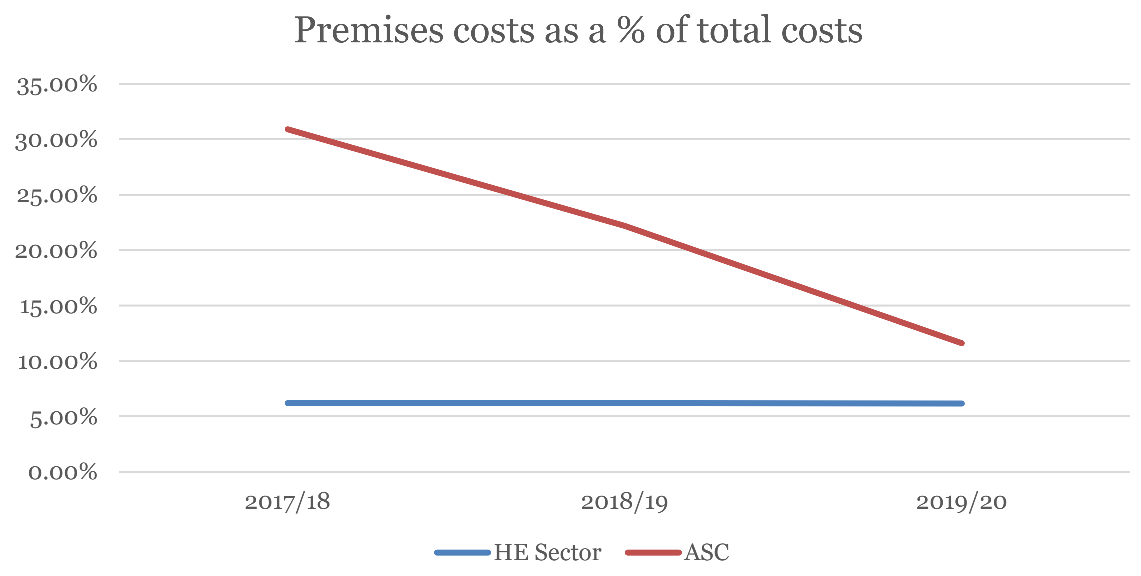
The above ratio indicates staff cost as a percentage of income/revenue. A lower staff costs against the peer is indicative of better managed institution. As per the analysis above the College's staff costs as a percentage of income improved from 26.0% to 15.6% during the course of period, which if compared to the HE sector average. This indicates that the College is utilising their staff more efficiently as compared against both sectors and the drop in percentage year-on-year indicates an improvement in management. Although, we understand from the management plans, that it is committed to increase its spending on staff costs close to the HE sector, once it is approved for public funding.

c) *Premises costs as a % of total costs*

Table 3:

Premises costs as a % of total costs	2017/18	2018/19	2019/20
HE Sector	6.18%	6.19%	6.16%
ASC	30.9%	22.2%	11.6%

Figure 3:



Current Performance Indicator: Below HE Sector

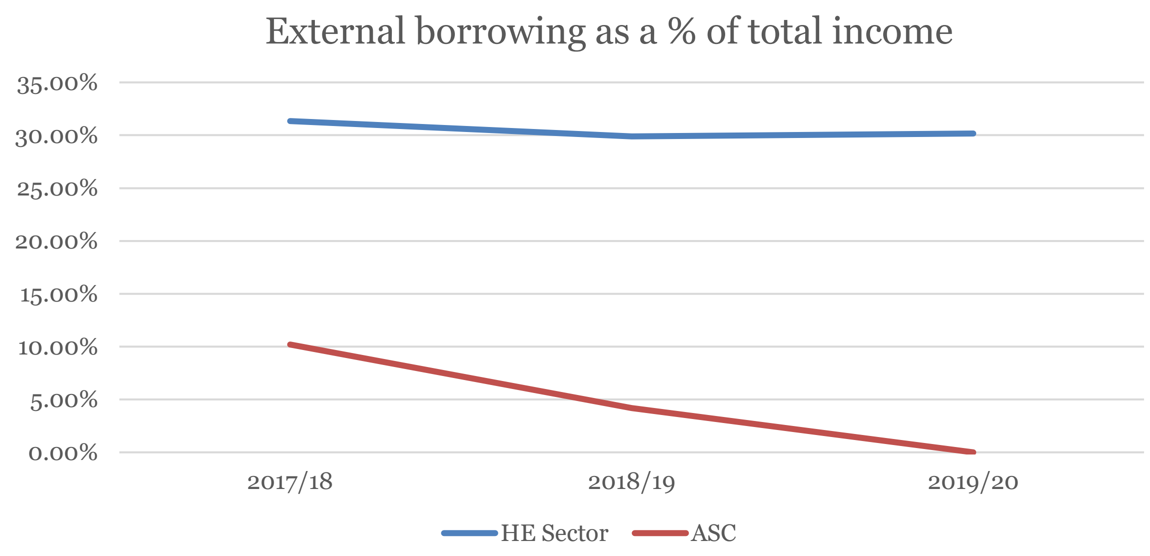
The above ration calculates the premises costs as a % of the total costs.

d) External borrowing as a % of total income

Table 4:

External borrowing as a % of total income	2017/18	2018/19	2019/20
HE Sector	31.34%	29.89%	30.17%
ASC	10.2%	4.2%	0%

Figure 4:



Current Performance Indicator: Positive better than HE Sector

The higher the level of borrowing (gearing) the higher are the risks to a business, since the payment of interest and repayment of debts are not "optional" in the same way as dividends.

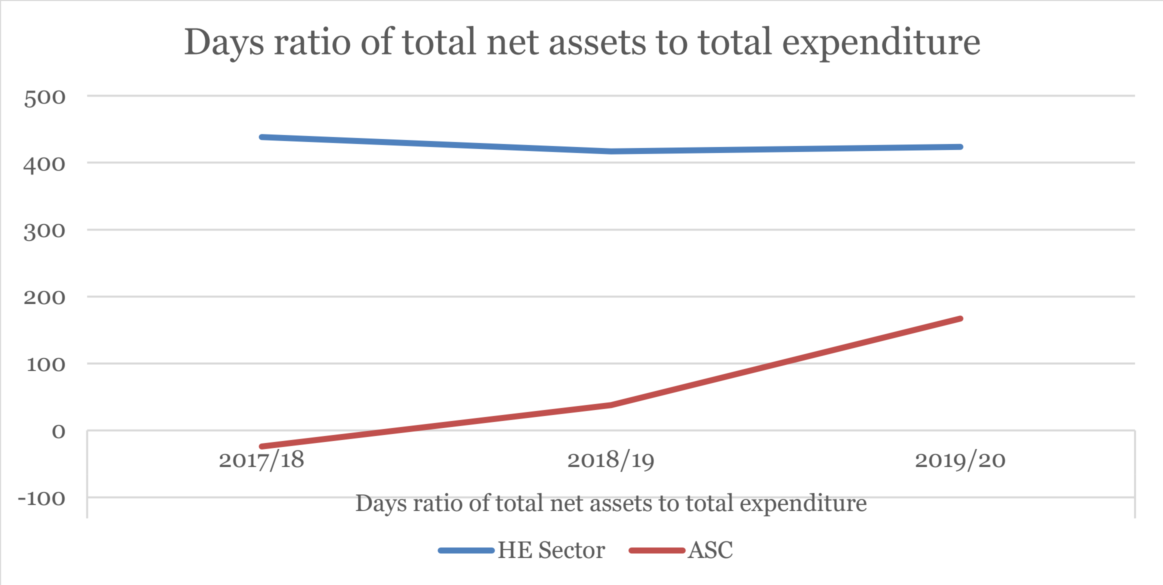
As Angelo College is debt free the ratio is nil and as compared to the HE sector is in a better position as it has not got an obligation to pay interest and repayment of debt. Also, due to its debt free nature, the College has not got any covenants to meet.

e) Days ratio of total net assets to total expenditure

Table 5:

Days ratio of total net assets to total expenditure	2017/18	2018/19	2019/20
HE Sector	438.28	416.88	423.70
ASC	(24.0)	37.9	167.10

Figure 5:



Current Performance Indicator: Below HE Sector

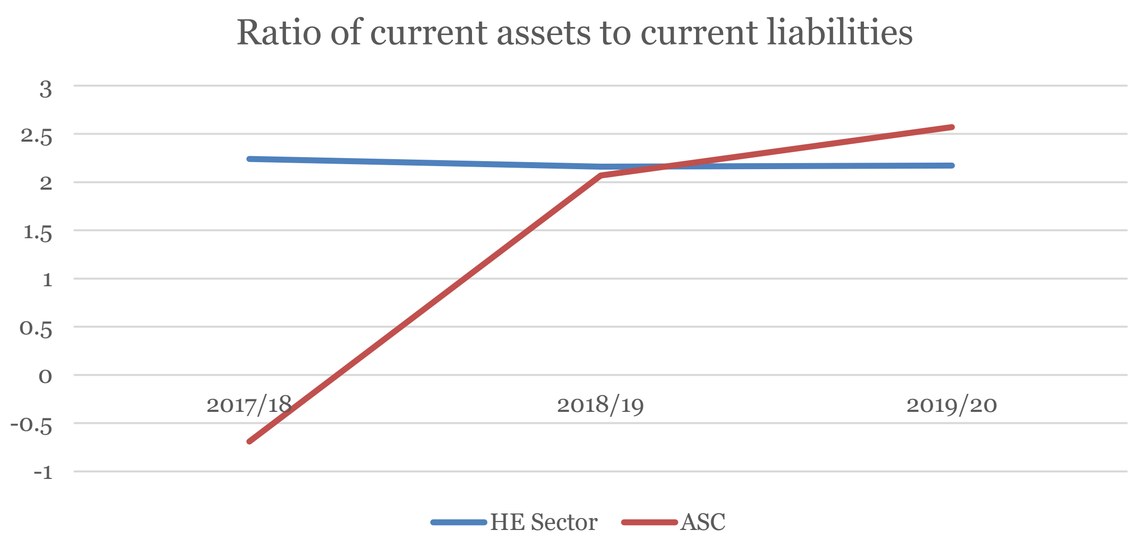
This ratio calculates the net assets to the total expenditure, meaning number of days an institution can survive without getting any further income. The days are well below HE sector but have significantly improved at the college level, which is a positive trend. It will continue to improve as the college grows.

f) Ratio of current assets to current liabilities

Table 6:

Ratio of current assets to current liabilities	2017/18	2018/19	2019/20
HE Sector	2.24	2.16	2.17
ASC	(0.69)	2.07	2.572

Figure 6:



Current Performance Indicator: Positive better than HE Sector

The current ratio is the measure of liquidity. It indicates whether the business can pay debts due within one year out of the current assets. The current ratio reveals how much “cover” the business has for every £1 that is owed by the company.

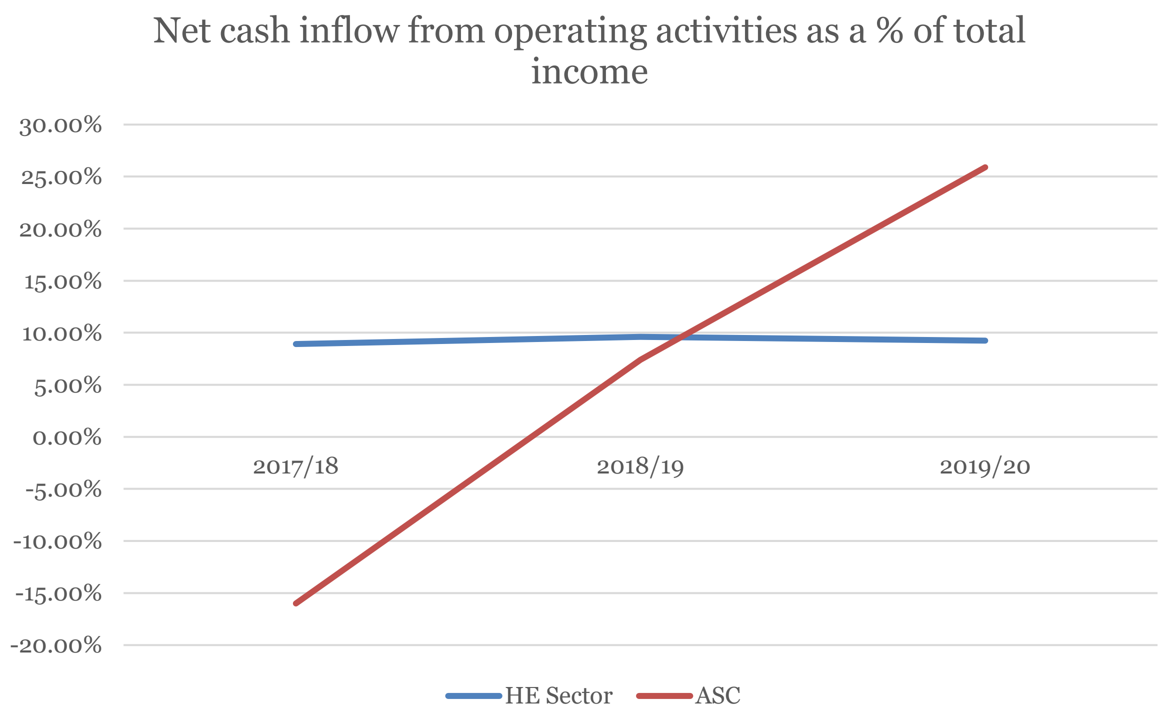
The above table shows that the College has improved significantly from 2017 to 2020 where the cover has increased to 2.57 times of the short term liabilities. This is significantly higher than the sector’s average of 2.17 which indicates the financial strength and liquidity of the College.

g) *Net cash inflows from operating activities as a % of income*

Table 7:

Net cash inflows from operating activities as a % of income	2017/18	2018/19	2019/20
HE Sector	8.92%	9.61%	9.24%
ASC	-16.0%	7.4%	25.9%

Figure 7:



Current Performance Indicator: Positive better than HE Sector

This ratio considers the relationship between cash generated from operating activities and total income in a company. A low ratio compared to industry may mean that your competitors have found a way to operate more efficiently.

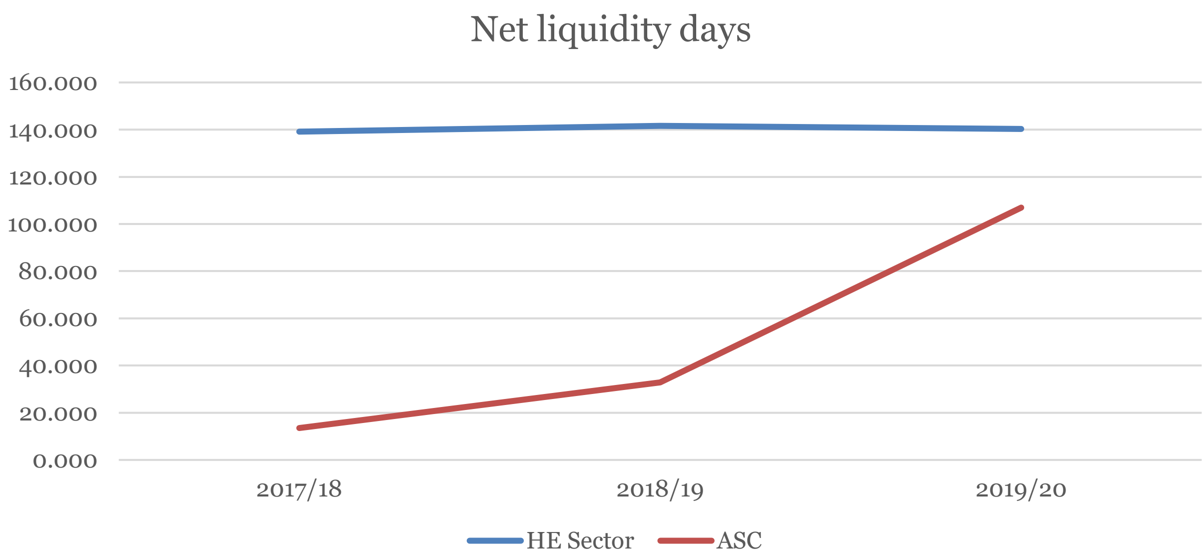
The above table shows that the cash from operations have again significantly improved and well above the HE sector of 9.24%. This shows that College is making effectively managing the business and generating significantly higher cash from operations as compared to the HE sector.

h) Net Liquidity days

Table 8:

Net liquidity days	2017/18	2018/19	2019/20
HE Sector	139.15	141.61	140.27
ASC	13.52	32.80	106.95

Figure 8:



Current Performance Indicator: Below HE Sector

Day's ratio of net liquidity to total expenditure (excluding depreciation) is calculated by taking numerator as Liquid Investments plus Cash at bank in hand minus current bank overdrafts and denominator as total expenditure excluding depreciation. The ratio represents how many days an institution can survive with its liquid and cash reserves.

The above ratio shows that the College has significantly improved and strengthen its liquidity position from 13.52 days to 106.95 days, which is while below the HE average of 140.27, but significantly improved This again is another indicator of the financial strength of the College and the ability to meet its expenditure through cash reserves.

6. Conclusion

This independent Review was commissioned by Anglo Skills College and our role has been essentially to review ASC's current financial strengths, assess any symptoms of overtrading and whether it is financially adaptable under different business scenarios.

Based on the information provided and the analysis above, our findings are:

1. Anglo Skills College is in a financially sound position.
2. With reference to benchmark used, the College is in a significantly stronger position as compared to other institutions in the HE from a operating point of view and has shown improvements in areas where it is currently below the HE sector.
3. The college is operationally in a sustainable position and is showing positive signs of improvements and growth.