IS STUDENT LOAN DEBT THE NEXT ECONOMIC BUBBLE IN THE EDUCATION INDUSTRY?

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ABSTRACT

Over the last decade, the U.S. economy has seen economic bubbles in the dot com and housing industries. Could education be the next bubble on the horizon? Currently, student loan debt surpasses total consumer debt and as of March 2012, student loan debt exceeds $1 trillion dollars. The focus of this paper is to aid in preparing students for successful student loan debt repayment. The content included discusses strategies to aid students in avoiding student loan delinquency or default in an effort to enhance student engagement and learning.

INTRODUCTION

Many who pursue higher education and professional certification require a monetary subsidy. Saving to finance higher education takes a longer time than borrowing to finance higher education. As a result of life happening, the repayment of the student loan(s) is more difficult than imagined at the time of borrowing(s). This paper is a literature review of current U. S. student loan indebtedness status and best practices for informed borrowing and repayment of student loans. It includes no discussion of saying "no" to university matriculation.

THE PROBLEM

In a highly competitive job market, persons are constantly looking for ways to distinguish themselves from the masses. A common approach is to seek additional education to more effectively compete in the global marketplace. It has been widely reported that the decision to complete an undergraduate education enhances one's lifetime earning potential by $1 million with a person completing a bachelor degree earning approximately $2.4 million over a 40 year work life. http://www.census.gov/prod/2012pubs/acsbr11-04.pdf (12/10/12).

In an effort to maximize educational attainment for greater earning potential, the average person is faced with the decision on how to finance their higher education. Unfortunately, the cost of higher education has been on the rise for some time. The 2011 Trends in College Pricing reports that over the last decade from 2001 – 02 to 2011-12, published tuition and fees for in-state students at public four-year colleges and universities increased at an average of 5.6% per year beyond the rate of general inflation. This rate of increase compares to 4.5% per year in the 1980s and 3.2% per year in the 1990s. http://trends.collegeboard.org/sites/default/files/College_Pricing_2011.pdf (12/10/12). *Figure 1* illustrates the annual percentage increases in tuition costs across 4 –year public and private colleges and universities as well as public 2-year colleges.

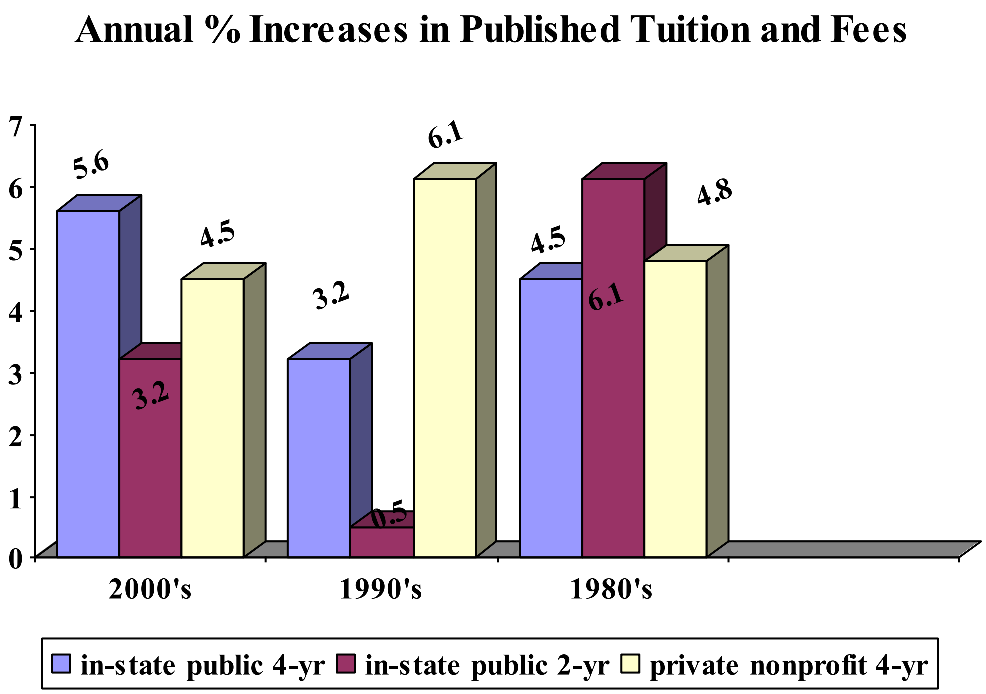

Figure 1- ***Data Source*****: 2011 Trends in College Pricing ; http://trends.collegeboard.org/sites/default/files/College_Pricing_2011.pdf (12/10/12).**

The challenge that the current college student faces is the disturbing recent trend in educational funding where the out of pocket college educational costs grow faster than incomes and has the potential to price out low to medium income families from earning a college education.

http://money.cnn.com/2011/06/13/news/economy/college_tuition_middle_class/index.htm (12/10/12).

Furthermore, this shifts the cost burden from the government subsidization model whereby higher education funding for state colleges and universities was supported by states in the budget appropriations process. In the 2011 Trends in College Pricing, state appropriations were reviewed and the findings indicate state funding per full-time equivalent (FTE) student for higher education institutions was 23% lower in inflation-adjusted dollars in 2010-11 than a decade earlier. Though the state funding declined, the costs increased. Average tuition and fees rose by 7% beyond inflation in 2010-11 slightly down from 9% in 2009-10. *Figure 2* illustrates the decline in state funding since 2008 through 2011. http://trends.collegeboard.org/sites/default/files/College_Pricing_2011.pdf (12/10/12).

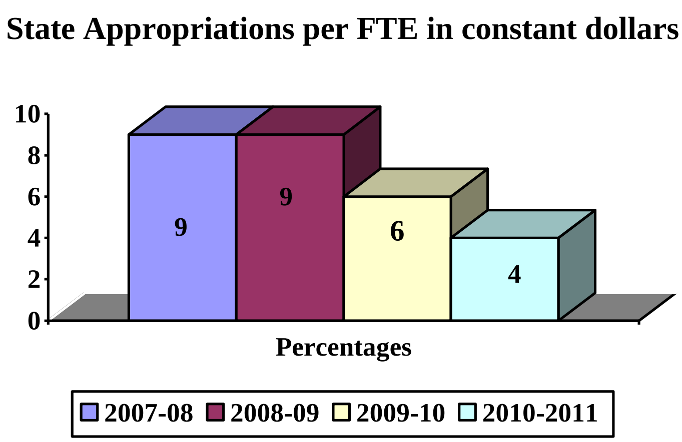

Figure 2 – *Data Source:* 2011 Trends in College Pricing; http://trends.collegeboard.org/sites/default/files/College_Pricing_2011.pdf (12/10/12).

As reported in the Economist, college fees have risen faster than inflation over the years. The per student cost of college has risen by nearly five times the rate of inflation since 1983. This type of increase in higher education continues to carve out a larger share of earner's income. The impact on median income is significant with sizable increases in the cost of a university education from 2001 through 2010 rising 15% from 23% to 38%. Heller, Donald. (2012). Higher education: Not what it used to be. ***The Economist***, (12/01/2012, print edition), 29 -30. As reported in a CNN Money article, *Surging college costs price out the middle class*, many middle class families have determined that college is becoming too expensive thereby limiting access to higher education. This is a growing problem because income levels have not kept pace with rising college costs. The CNN Money article also reported that in 2008, the median income was $33,000, far below the $77,000 annual estimate if incomes had grown as fast as college costs.

http://money.cnn.com/2011/06/13/news/economy/college_tuition_middle_class/index.htm (12/10/12). Such increases leave college students with the need for supplemental educational funding. Tom Hayden writes from the Chronicle of Higher Education, "students today …even those that hold part-time jobs – fall tens of thousands of dollars in debt." Hayden, T. (2010). We can't afford to be quiet about the rising costs of college. ***The Chronicle of Higher Education***, 56, 29-31. Over the past 15 years the debt per student has doubled. Those graduating from undergraduate school carry student loan debt with two-thirds having taken out student loans. Such high numbers of college students carrying student loans is alarming considering the chance of an American college student completing an undergraduate degree in six years is only about 57%. Heller, Donald. (2012). Higher education: Not what it used to be. ***The Economist***, (12/01/2012, print edition), 29 -30.

Yet the elevated student loan levels may have a lasting impact on the national economy. The national study by the Pew Institute found that one of five US households (19%) owed student loan debt in 2010, a 4% increase since 2007. The study also found that 40% of all households headed by someone 35 years old or younger owed student loan debt. Additionally, findings show that among household's owing student loan debt, the average outstanding student loan balance increased (14%) from $23,349 in 2007 to $26,682 in 2010. The debt load of the average public four-year college graduate was $22,000 (in 2010 dollars) up 6.82% from $20,500 (2010 dollars) in 2006 – 2007. (www.pewsocialtrends.org) Pew Institute and Survey of Consumer Finances (11/5/12)

As of 2012, the national impact of student loan debt hit an historical number when the Consumer Financial Protection Bureau reported student loan debt surpassed $1 trillion which is more than credit card debt nationally.

http://www.forbes.com/sites/moneywisewomen/2012/08/29/3-reasons-to-never-default-on-your-federal-student-loan/ (11/6/12). Such a significant amount of educational debt causes concern about sustainability for the overall economy as well as the long-term impact on the individual borrower.

Each year, the Department of Education (DOE) releases data on the manageability of student loan debt, this section will summarize the most recent data available on student loan repayment and default rates. A March 2011 report by the Institute of Higher Education Policy found that only 37% of borrowers who started repaying their student loans in 2005 were able to pay them back fully on time. The report examined "more than 8.7 million borrowers with almost 27.5 million loans who started repayment between October 1, 2004 and September 30, 2009." (IHEP 2011). The report served as "a snapshot of borrower experiences" from repayment and steps to "avoid delinquency and default." The Department of Education data on default rates is included but first a good understanding of what options are available to students need some attention. Loan delinquency occurs when payments are not made within 60 days of the due date and a loan is considered in default if borrowers exceed 270 days of delinquency. (IHEP 2011).

The U.S. Department of Education recently released the fiscal year (FY) 2010 cohort consisting of borrowers whose first loan repayments came due between Oct. 1, 2009, and Sept. 30, 2010, and who defaulted before Sept. 30, 2011. Almost 375,000 borrowers defaulted for an average of 9.1 percent from more than 4.1 million borrowers. The current default rate for FY 2010 is 9.1% up from 8.8% in FY 2009 rising from 7.0% in FY 2008. http://www.ed.gov/news/press-releases/default-rates-rise-federal-student-loans (11/06/12).

Figure 3 illustrates the default rates by institution type form FY 2008 through FY 2010.

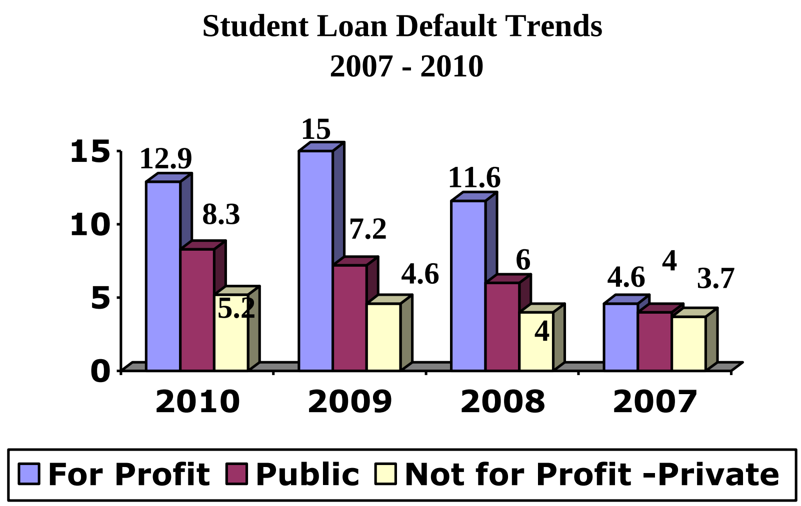

Figure 3 – *Data Source:* Dept. Education http://www.ed.gov/news/press-releases/first-official-three-year-student-loan-default-rates-published(11/07/12)

In September 2012, the Department of Education introduced the use of the new three year default rate, DOE is switching to a 3-yr measurement as required by the Higher Education Opportunity Act of 2008. As a result the implementation of the Higher Education Opportunity Act, the 2012 report will have both two year as well as three year default data. DOE reported the FY 2009, three-year federal student loan default rates was 13.4% nationally. An overview by institution type includes 11% for public institutions; 7.5% for private non-profit institutions and 22.7% at for-profit schools. http://www.ed.gov/news/press-releases/first-official-three-year-student-loan-default-rates-published (11/07/12)

Individual borrowers are not the only parties that the DOE keeps tabs on. Educational institutions are also monitored for borrowing patterns of its students. The Department of Education will sanction schools if the school's default rate exceeds 25% for three consecutive years, exceeds 40% in the latest year or both occur. Additionally, schools with excessive default rates may lose their eligibility in one or more federal aid programs. Finally, a quick review of the local performance of schools in Houston is provided. The default rates for universities ranged from 23.9% to 8.8% for public institutions and 7% to 2.1% for private non-profit schools. Figure 4 illustrates the local outlook for colleges and universities within the Houston area.

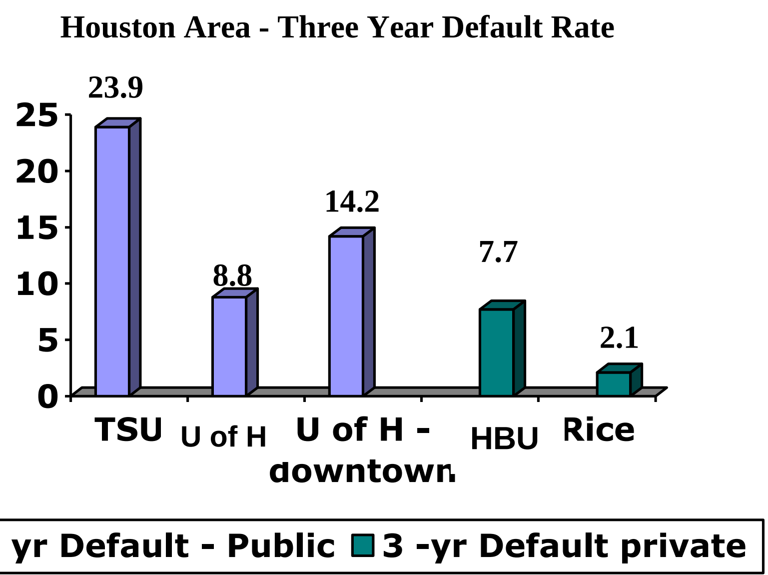

Figure 4 - *Data Source:* Houston Chronicle http://www.chron.com/news/houston-texas/article/Student-loan-defaults-on-the-rise-3904101.php (11/06/12)

STUDENT LOAN(S) PLANNING BEST PRACTICES

The Federal Student Loan Program was created for the purpose of increasing the menu of affordable funding sources for students who are pursuing under-graduate and or graduate degrees or professional certifications. For many, the system is working as it was created to work: borrowers completed their respective degree requirements or certification requirements, became or continued to be gainfully employed, and have repaid or are repaying their loan(s) in accordance with the terms of their loan(s) agreement(s). According to (IHEP 2011), this grouping of student loan borrowers comprises one-third of the 2005 repayment cohort population of this study. "This report examines the repayment experiences of student loan borrowers using data provided by five of the largest student loan guaranty agencies. The primary focus is on the nearly 1.8 million borrowers who entered repayment in 2005". The IHEP 2011 study focused on borrower repayment patterns and included those who were trying to meet their repayment obligations—within the first five years of repayment-- and who

> 1. " made timely and expected progression,
> 2. became delinquent during the study and debt repayment periods, and
> 3. used various options to postpone or delay repayment." (IHEP 2011).

This section addresses the fast growing remaining segment of the student loan population who may/may not have earned under-graduate and or graduate degrees; who may/may not have completed professional certification requirements; who may/may not be gainfully employed and they are not repaying their student loan(s) in accordance with the terms of their loan(s) agreement(s). (IHEP 2011).

Some Characteristics of Those Borrowers For Whom The Federal Student Loan System Is Working As Planned

First, goal-oriented student loan borrowers were familiar with the repayment options' provisions available to them during the period of their debt repayment. Second, they understood the concept of borrowing: contractual loan terminology, interest accrual, life of the loan, installment payments, and they had received assistance in choosing a loan repayment plan. Third, they were engaged in liquidating their loan balance(s) so they timely filed the paperwork necessary to avoid delinquency that would result in default. Fourth, it was important to these borrowers that they would avoid the consequences of student loan repayment defaulting: inability to use the Form 1040 Earned Income Credit, wage garnishment up to a maximum of 15%, Social Security benefits garnishment, depression, limited career choices, and the delaying of marriage and home purchasing to name a few. Fifth, it seems the older the borrower, the higher the loan repayment frequency. (IHEP 2011). As of September 18, 2012, people 60 and over owed $43 billion for student loans. http://www.businessweek.com. (10/18/2012).

From a public policy view, the IHEP 2011 study suggested that student success should be defined according to the following three factors: access to higher education; persistence to degree completion or to certificate completion; and effective student loan debt management.

Accountability of Borrowing Students

This section addresses student training in, and monitoring of, effective student loan debt management. The web address, below, of the Federal Student Aid Office of The U. S. Department of Education leads to information about the following topics at the following links:

Making Payments
Loan Servicers
Repayment Plans
Loan Consolidation
Deferment and Forbearance
Forgiveness, Cancellation, and Discharge

Understanding Default
Resolving Disputes

Here, both before and after incurring debt, expect to access all the official information one needs to manage repayment of one's federal student loans. http://studentaid.ed.gov/repay-loans (12/20/2012)

The following websites are ones that students should visit at least once a month beginning their junior year in high school and continuing through the completion of their undergraduate degrees or certification programs:

1. Debt Rule of Thumb. Avoid creating debt if at all possible. "The number one rule of thumb is that a student should not borrow more than his/her expected first year salary upon graduation. Repayment for college can last 15 years after graduation, consideration for both the financial futures of the parents and students should be given." . . . Parents or guardians, " if you are in doubt and have questions, call upon the Financial Aid office located at your student's college of choice." http://blog.collegeplanningservices.org/my-blog/2011/03/borrowing-for-college-tuition.html (12/12/2012).

2. Some Sources of Free Money. *Kantrowitz's article discusses the need to minimize student loan debt and provides more than a dozen practical tips on ways to reduce borrowing to pay college costs*. It provides a link to loans, banking benefits and student deals with Simple Tuition. Without ceasing, both students and their parents are urged to search and apply for scholarship funding. Following this author's advice will help borrowers to "Live like a student while you are in school so you don't have to live like a student after you graduate." http://www.fastweb.com/financial-aid/articles/3092-how-to-minimize-student-loan-debt (12/12/2012).
3. Cast Down Your Bucket Where You Are. Regarding *Borrowing for College* , Author Eugene Meyer reports the advice of a student loan borrower to her younger sister: "I think you have to take a hard look at what you think you will earn with what you are studying." The older sister is repaying $165,000 in student loans at the rate of $1,100 per month. The younger sister listened and is now enrolled at one of her state's public universities.

http://www.usnews.com/education/best-colleges/paying-for-college/articles/2011/09/20/think-hard-before-borrowing-for-college (12/10/2012). The most critical variable in attaining higher education success is the student—not the professors, not the prestige of the university, and not the location of the university. If higher education funding is an issue for a student, then the student should matriculate at an affordable university such as at Little Rabbit University. The more the student embraces Little Rabbit University's resources and offerings, the more Little Rabbit University will embrace the student.

4. Use Home University's Calculator. "By the end of October 2011, U.S. colleges will be required to post a "net price calculator" on their websites to allow prospective students to see an estimate of the true amount they'll owe and will have to borrow." This calculator should be custom-made for each university as opposed to being a generic one. thttp://www.usnews.com/education/blogs/the-college-

solution/2010/07/13/use-an-aid-calculator-to-get-the-real-cost-of-college (12/11/2012)

Accountability of Colleges and Universities

The table below shows the classifications of the 218 institutions that had "three-year default rates above 30 percent; 37 of these institutions had three-year default rates higher than 40 percent." Beginning in September 2014, colleges and universities will face sanctions--"ineligibility for federal student aid if their default rate is 30 percent or greater for three consecutive years or exceeds 40 percent in a single year."

Table 1: Institutions Having Above 30% Default Rates as of September 28, 2012

Colleges	Total	HBCUs	Percentages
For Profit	160		
Public	35	3	9%
Private	23	11	48%
Total	218	14	

Table Data Source: http://chronicle.com/article/Default-Rate-on-federal/134786 (12/10/2012).

"We continue to be concerned about default rates and want to ensure that all borrowers have the tools to manage their debt," said U. S. Secretary of Education Arne Duncan. "In Addition to helping borrowers, we will also hold schools accountable for ensuring their students are not saddled with unmanageable student loan debt." How are Colleges being held accountable? Source: www.ed.gov/news/press-releases/first-official-three-year-student-loan-default-rates-
(12/12/2012).

Should colleges be given the ability to limit their students' borrowing? This provision already exists. For example, the maximum loan amount for a Direct Plus Loan is the student's cost of attendance (determined by the school) minus any other financial aid received. http://studentaid.ed.gov/types/loans/plus. (12/20/2012). The following partial table lists some of the universities that either disallows student loans or limits them. This is only a part of the original Table and is here labeled as Table 2.

Table 2: Summary of Pledges: Eligibility Guidelines and Basic Provisions (2009-10)

Pledges Covering Entire Cost of Attendance, http://studentaid.ed.gov/types/loans/plus. (12/20/2012).

Institution	**Maximum Family Income**	**Role of Loans in Covering Calculated Need***
Amherst College	No Income Limit	No Loans
Bowdoin College	No Income Limit	No Loans
Brown University	$100,000 / No Income Limit	No Loans/ Loan Limits
California Institute of Technology	$60,000	No Loans
Claremont McKenna College	No Income Limit	No Loans
Colby College	No Income Limit	No Loans
College of William and Mary	$40,000†	No Loans
Columbia University	$50,000	No Loans
Connecticut College	$50,000 / $75,000	No Loans / Loan Limits
Cornell University	$75,000 / $120,000	No Loans / Loan Limits
Dartmouth College**	No Income Limit	No Loans
Davidson College	No Income Limit	No Loans
Duke University	$40,000 / No Income Limit	No Loans / Loan Limits
Emory University	$50,000 / $100,000	No Loans / Loan Limits
Georgia Institute of	$33,300†	No Loans

Pledges Covering Entire Cost of Attendance, http://studentaid.ed.gov/types/loans/plus. (12/20/2012).		
Institution	**Maximum Family Income**	**Role of Loans in Covering Calculated Need***
Technology		
Grinnell College	No Income Limit	Loan Limits
Harvard University	No Income Limit	No Loans
Haverford College	No Income Limit	No Loans
Indiana University, Bloomington	185% of Federal Poverty Level‡	No Loans
Lafayette College	$50,000 / $100,000	No Loans / Loan Limits
Lehigh College	$50,000 / $75,000	No Loans / Loan Limits
Massachusetts Institute of Technology	$75,000 / No Income Limit	No Loans / Loan Limits
Middlebury College	No Income Limit	Loan Limits
North Carolina State University	150% of Federal Poverty Level‡	Loan Limits
Northwestern University	EFC Less than 20% of COA / No Income Limit	No Loan / Loan Limits

* All of the institutions listed require some student contribution of earnings from academic year work, usually a federal work-study job or summer work. Also, some families may need to borrow to cover any expected family contribution (EFC), even if the institution does not include loans in the financial aid package.

† In-state students only

** Starting with incoming freshmen in 2011-12, Dartmouth College will re-introduce loans of $2,500 to $5,500 per year for students with family incomes above $75,000. See "Dartmouth Board of Trustees approves measures to close $100 million budget gap." Source: http://projectonstudentdebt.org/Type_and_Coverage.vp.html. (12/21/2012).

SUMMARY

Student loans are real loans and they must be repaid. Students and parents should become informed about the menu of educational financing opportunities—including their costs. Borrowers should not be allowed to borrow more than they can repay based on their assets and reasonable expectations of earned income. "Repayment for college can last 15 years after graduation; consideration for both the financial futures of the parents and students should be given." http://blog.collegeplanningservices.org/my-blog/2011/03/borrowing-for-college-tuition.html. (12/21/2012).

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U. S. Department of Education. *PLUS loans are federal loans that graduate students and parents of dependent undergraduate students can use to help pay for college or career school.* Available at: http://studentaid.ed.gov/types/loans/plus.

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